Education Property Tax Changes to Create A Growth Agenda for Saskatchewan

Submission by the Greater Saskatoon Chamber of Commerce and Regina and District Chamber of Commerce

October 2009

Education Property Tax Committee

Research Advisory Committee

The following individuals devoted their time and effort to this common project of the Regina and Saskatoon Chambers of Commerce as volunteers. Our appreciation is also addressed to Canada West Foundation for devoting the time of Jack Vicq.

The Research Advisory Committee is made up of Jack Vicq, Randy Jeworski, Herve Langlois, and Rhonda Speiss.

Jack Vicq

Jack Vicq is presently the Director of the Saskatchewan office of the Canada West Foundation and Professor Emeritus of Accounting at the Edwards School of Business, University of Saskatchewan. He holds a Bachelors Degree of Commerce in Accounting and a Masters Degree of Science in Accounting. Mr. Vicq is a retired professor of Accounting and former Associate Dean in Commerce at the University of Saskatchewan. He is the former Director of the Centre for International Business Studies at the University of Saskatchewan.

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Vicq headed the Provincial Income Tax Review Committee in 1999 and presented the *Saskatchewan Personal Tax Review Committee Report* to the Saskatchewan government. During 2002-2005, he was the chairperson of the Provincial Court Commission. Most recently, he chaired the Business Tax Review Committee for the Province of Saskatchewan. Jack was a member of the Board of Directors of PotashCorp and chair of the Audit Committee until 2007. He currently sits on two not- for-profit boards.

Randy Jeworski

Randy is a graduate of the University of Regina (1995). He also has accreditation as a Municipal Assessment Valuator. Randy worked for 19 years for Municipal Government in Regina in the areas of property valuations and tax administration. Having been involved in property valuations and property taxation policy and administration since 1977. He has a strong knowledge of all the aspects of taxation on property and how valuations are derived in Saskatchewan.

In 1996, he joined a private company and began consulting for commercial and industrial property owners to help them understand the correctness of their property tax values. For 6 years he served many of the largest property owners or real estate managers. He currently looks after marketplace growth and eminence programs for Deloitte.

In 1997 Randy joined the Regina and District Chamber of Commerce as a committee member, soon was asked to let his name stand for Director/Board member and then in 2004 was elected to the Executive. On January 18, 2007, the Regina and District Chamber of Commerce inducted its 121st President, Mr. Randy Jeworski. Mr. Jeworski has been a life long Regina-area resident, so he knows the city and province well and is passionate about improving Regina's business community, as well as working with others to grow the province.

Herve Langlois

Herve Langlois has been a resident of Saskatoon since 1976. He attended the University of Saskatchewan, obtaining his Bachelor of Arts, Bachelor of Education and Masters of Education. He also attained a Ph.D from the University of Oregon. He later returned to the University of Saskatchewan as an adjunct professor and sessional lecturer.

He served as a Saskatoon city councilor from 1994 to 1997, as a Deputy Director of Education with the Saskatoon Public Schools (1976-93) and as chairman with the Saskatchewan School Finance and Governance Review. He has also previously served on the Saskatoon Board of Trade, the Saskatchewan Assessment Management Agency Board of Directors and the Saskatchewan Local Government Finance Commission. From 2000 to 2005, Mr. Langlois acted as an international consultant with the Inter-American Development Bank on projects in Jamaica, Bahamas, and Guyana.

Rhonda Speiss

Rhonda was elected to the Board of Directors of the Greater Saskatoon Chamber of Commerce in 2009. She has 13 years of experience in the fertilizer industry as well as several years of experience as a small business owner in Saskatchewan. As an entrepreneur, Rhonda has considerable experience in several markets, including agri-business, specialty food marketing and yard maintenance. As PotashCorp's Manager of Public Relations since 2004, Rhonda is a spokesperson for the corporation. She oversees the design, content and operation of the corporation's award winning website and also oversees one of the most highly visible corporate donations programs in Saskatoon. Previously, as Manager of Market Research, she tracked and reported on markets vital to PotashCorp's operations.

Serving her community, Rhonda is a member of the Royal University Hospital Royal Ball Organizing Committee and was a member of the Marketing Committee for the 2007 Juno Awards, held in Saskatoon. Rhonda earned a Bachelor of Commerce degree from the University of Saskatchewan and a Business Administration diploma from Assiniboine Community College in Brandon, Manitoba.

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The Saskatoon & District Chamber of Commerce would like to express its gratitude to The Canada West Foundation for the financial contribution toward an honorarium for the research assistants.

Executive Summary

Property taxes rank poorly in terms of good taxation policy because they are a discriminatory wealth or capital tax. Because of its perpetual nature and insensitivity to profit (you have to pay it whether you're making money or not), property tax has a significant effect on investment decisions. Jurisdictions seeking to attract investment capital must offer very competitive property tax rates. Capital taxes are being dropped in most countries because they discourage investment.

In 2009, the Saskatchewan provincial government reformed its province-wide education property tax system. Even within these changes, there are five different mill rates: residential, farmland and three categories of commercial property, each multiplied by differing percentages to calculate the taxable assessment (and differing mill rate factors for the municipal portion). The resulting taxable value is not transparent to property taxpayers.

The Saskatchewan government's reason for changing the education property tax system was to encourage investment in the province. These changes were a step in the right direction but competing provinces like Alberta still have superior tax structures from both a transparency and competitiveness perspective. In Alberta there are only two education mill rates for all property categories: 3.39 for residential and agricultural property and 4.98 for non-residential property. This is simple, transparent and competitive. In contrast, Saskatchewan's education property tax mill rates can be up to 18.28 for non-residential property. Alberta's competitive advantage is obvious.

Frequency of assessment also helps Alberta stay competitive. In Alberta, reassessment occurs every year. Saskatchewan's four-year reassessment cycle creates a lag time that can stretch as long as seven years, adding a further layer of complexity and confusion to the Saskatchewan system. This has resulted in substantial differences between the nominal assessment which is established every four years. At establishment, this is already three years out of date and grows to seven years out of date before the next valuation. This time lag is addressed in this report by referring to the nominal tax rate and the effective tax rate. The nominal mill rate is the stated rate in the 2009 reassessment and the 2009 budget. The effective rate adjusts the stated nominal mill rate to current (2009) effective mill rate.

To improve transparency and simplicity, at the next reassessment the province should:

i) Tax all properties on their entire assessed value (100 per cent assessed value)
ii) Make assessment cycles more frequent
iii) Set explicit, transparent policy objectives for setting different mill rates for farm investors and residential property owners.
iv) Eliminate the three-tier commercial mill rates as the other recommendations in this report are adopted.

To achieve these tasks over time, a gradual process of de-emphasizing property tax as a tax base for education will be required. Our projections show that this revenue will be replaced by an expanded tax base that will come from new investment as a result of improved competitiveness.

Income tax deductibility for non-residential assessment as compared to residential property only partially supports a mill rate differential between non-residential and other types of real property in Saskatchewan. Even if this argument is accepted, a maximum differential ratio of 1.43 can be justified. The 2010 residential mill rate of 9.51 represents this maximum premium if applied to non-residential properties at 100 per cent of the non-residential assessment because residential properties have a taxable assessment of only 70 per cent of their property assessment and this 100 per cent to 70 per cent assessment inclusion ratio for taxable assessment purposes is equivalent to a 1.43 ratio.

Marginal effective tax rates (METR) are a significant factor in business investment decisions. The education property tax has a relatively high influence on METR and is therefore negatively affecting business investment in Saskatchewan. METR measures the additional rate of return on an investment that is required to pay the tax and still generate the required investment return. This report includes the education property tax collected in Saskatchewan and Alberta in calculating the METR to determine the extent of the impact of the education property tax on investment decisions.

A business seeking an after-tax return of 12 per cent needs to see a before-tax rate of return of 18.3 per cent in Saskatchewan but only 15.8 per cent in Alberta. On a $5 million project, the Saskatchewan location would require an additional $125,000 annually of before-tax income.

This analysis is supported by the results and conclusions of several previous reports and studies on property tax such as the one commissioned by the City of Saskatoon in 1997. The analysis is further supported through detailed modeling of the 2008 KPMG *Competitive Alternatives* study.

More detailed analysis of the KPMG model shows that factory expansion in Saskatchewan is even more adversely affected by the province's stepped commercial mill rates. A $1.9 billion oil upgrader built in Saskatchewan rather than Alberta pays a $16,626,857 property tax premium on an effective tax basis and $25,764,450 on a nominal basis per year in property tax.

Saskatchewan has several recent examples of increased business investment because of improvements in taxation competitiveness:

- The policy change by the City of Saskatoon in 2001, limiting the effective tax rate on commercial property from 2.11 to 1.75 times the residential effective rate, led to a growth in the total commercial and industrial assessment from $7,540 per capita in 2001 to $10,014 per capita in 2007. Since 2007, this has grown to $13,255 per capita. On an effective basis the 2009 non-residential assessment per capita has grown to $17,227 per capita.

- In 2002, the province reduced the corporate capital tax resource surcharge on new production. From 1995 to 2005, employment in that sector increased from approximately 17,000 to 25,000.

Non-residential property investments are the foundation upon which a province's tax base is built. The non-residential assessment base in Saskatchewan is substantially smaller on a per capita basis than in Alberta, despite the very similar attributes of the resource bases of the two provinces. The

2009 non-residential assessment base is approximately $129 billion in Alberta compared to $18 billion in Saskatchewan. On a per capita basis, the non-residential per capita assessment base of Alberta is over $35,500 while it is under $18,000 in Saskatchewan.

Saskatchewan can, over time, match Alberta's non-residential per capita property assessment. This assessment growth would generate significant new municipal property tax revenues and provide new provincial revenues from other forms of taxation. Property tax restructuring could attract billions or possibly even hundreds of billions of dollars of new investment. At a mill rate of 10, an additional $100 billion in non-residential assessment in Saskatchewan could result in $1 billion in incremental annual municipal property tax revenue.

The 2010 average non-residential education mill rate in Saskatchewan of 15.10 mills will generate approximately $273 million in tax revenue. A Saskatchewan non-residential mill rate of 7.47 mills would be required to generate the same $273 million in education property taxes if the non-residential assessment base in Saskatchewan achieved Alberta's per capita non-residential levels. This level would be much more competitive with the Alberta 2009 mill rate of 4.98 mills. To further close the mill rate gap between Alberta and Saskatchewan will require further funds from general revenues, but the significant growth in investment that this model projects would provide significant new provincial revenue to make this possible.

The economic growth resulting from these recommendations may occur quickly. When the City of Saskatoon reduced the property tax premium paid by non-residential taxpayers in 2001, growth in that city accelerated both in revenue, investment and career choices.

The wealth effect derived from a properly structured and competitive non-residential education mill rate can result in reduced municipal and library mill rates and improved services as the per capita non-residential assessment base in the province grows while boosting other sources of provincial revenue. This kind of growth was experienced by Red Deer, which generated $52 million in municipal property taxes in 2001 and over $102 million in 2008 while mill rates fell substantially.

With the exception of education property taxation and sales tax, Saskatchewan is a highly competitive jurisdiction for the industries used by KPMG in its *Competitive Alternatives* study. This makes it all the more likely that accelerated investment would result from property tax changes.

A Start on the Path to a Virtuous Cycle

Our Chambers will continue to advocate for improved property policies, taxation transparency and competitiveness in 2013, but in this report our Chambers challenge the provincial government to make an important growth-orientated interim tax structure change that will improve Saskatchewan's growth prospects and our competitiveness.

Because the new and more competitive mill rate included in our recommended measures will only apply to incremental taxable assessment, this policy change places no additional burden on the provincial treasury between today and the next reassessment, scheduled for 2013.

Five measures will make Saskatchewan competitive with Alberta in regards to education property taxes:

1. Apply a mill rate of 9.51 to all new or expanded non-residential property investment between now and the next reassessment.
2. Cap the amount of revenue received from the non-residential properties at the forecast 2010 revenue of $273.5 million until the province meets the Alberta non-residential mill rates in competitiveness.
3. Apply a mill rate of 9.51 mills (or lower if such a rate will still raise $273.5 million in non-residential education property taxes in 2013) to all non-residential property at a single rate at the next reassessment in 2013.
4. Reduce the non-residential mill rate on all new or expanded non-residential property to the residential rate to be applied at the 2013 reassessment (estimated in this report to be 7.36 mills) until the next reassessment (currently expected in 2017), and repeat this approach in 2017 if the changes are still insufficient to result in an Alberta-competitive non-residential education mill rate.
5. Consider applying additional general revenues to reduce the revenue required from non-residential properties in 2011, 2012 and 2013 to accelerate the process of building the assessment base.

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Regina Chamber Mission

"The Regina and District Chamber of Commerce is an independent member driven organization dedicated to fostering an environment in which our community prospers."

Saskatoon Chamber Mission

"Building the best business climate in Canada thereby creating a city of opportunity."

1. A Growth-Stimulating Education Property Tax Structure for Saskatchewan

This report demonstrates that:

1. Tax policy matters.
2. A properly designed property tax policy can encourage growth and investment.
3. Saskatchewan has not yet achieved a competitive education property tax level or structure. Changes made today can build the Saskatchewan economy for tomorrow.
4. The interim recommendations in this report can assist in improving the education property tax structure of Saskatchewan, promote investment and build the property assessment base of Saskatchewan without additional funding requirement from the provincial treasury. A future treasury demand may be required in 2013 at the next reassessment.
5. The interim recommendations contained in this report will serve as an important stimulus to business investment in Saskatchewan as the global economy struggles to recover from the deepest global recession in the post World War II period.

Business organizations in Regina and Saskatoon have been advocating for change in the property tax structure of Saskatchewan since at least 1981.

While some progress has been made to improve the structure and level of property taxation at the municipal and provincial level, more adjustments will be necessary to achieve a principle-based and competitive education property tax structure.

A quote from the Saskatchewan Party's 2005 submission to the Saskatchewan Business Tax Review Committee conveys the importance of a competitive education property tax regime:

"Property taxes are the largest tax on capital in Saskatchewan. The high rates at which business taxes are applied in Saskatchewan create a significant barrier to private sector investment growth, job creation and new capital investment. Any attempt by the province to evaluate and recommend changes to the mix of taxes and fees assessed against Saskatchewan businesses must include property taxes if it is to be effective."[1]

The Regina and Saskatoon Chambers' efforts since 1996 have been jointly focused on improving the accuracy, transparency and competitiveness of property taxes in the province. This study represents the first coordinated joint study undertaken by these organizations since their formation over 100 years ago.

In 1997, the City of Saskatoon created the Property Tax Review Committee in response to a consensus raised during the 1997 reassessment. Jack Vicq served as one of three of the city's Tax Review Committee representatives. Herve Langlois was a City of Saskatoon councillor at the time that this committee was established. Randy Jaworski assumed the position of city assessor in the City of Regina in 1999.

All three of these individuals have had long and distinguished careers of public service to their cities and this province. Following the recent changes to education property taxes, each of these well-respected citizens volunteered their time and considerable expertise to the Regina and

Saskatoon Chambers to undertake this joint project. Their driven commitment was derived from their significant knowledge of the intricacies and shortcomings of the Saskatchewan property assessment and taxation rules as embedded in the education property taxation system now in place.

They, along with the Greater Saskatoon Chamber of Commerce board member, Rhonda Speiss, have supervised the research, writing and editing of this report.

This study builds on the previous research undertaken by the Saskatoon and Regina Chambers and analyzes the rules implemented in Saskatchewan in 2009.

This report will provide historical, theoretical, anecdotal and empirical proof of the importance of a well-designed, principle-based and competitive property taxation system in terms of establishing a growth-encouraging education taxation policy in the province.

This study proposes an interim solution that will materially improve Saskatchewan's positioning toward attracting much needed investment stimulus without any cost to the Government of Saskatchewan.

2. Brief History of Education Component of Property Tax

Saskatchewan school divisions have been taxing local properties to fund education since 1905. Most of the burden of education funding has been placed on property owners. "In the past thirty years, the Provincial Government has not provided more than 60 per cent of the operating costs to boards of education."[2] The following is a breakdown of the last 34 years of education funding as divided between property taxes and the provincial government's general revenue sources. There is also an estimate for 2010.

Government vs. Property Owners' Share of Funding for Pre-Kindergarten to Grade 12 Education

Year	1975	1992	2004	2008	2009	2010
Property Tax Funding %	43	55	56	49	37	34
Government Funding %	57	45	44	51	63	66

As can be seen, there is a declining reliance on property taxes for education funding. The current government's promise in the last election campaign to "achieve a fairer balance for education funding, to ensure the education system is properly funded, and to reduce the education portion of property tax"[2] represented a commitment to continue this trend.

Prior to 1996, Saskatchewan used a single mill rate for all types of property. A mill rate is the tax per dollar of assessed value of property. One mill (rate is expressed in mills) is one-tenth of a cent ($0.001), but this changed to a more complex and less transparent system at the 1997 reassessment.

The different property classes in Saskatchewan include: residential, multi-unit residential, non-residential, seasonal residential, elevators, non-arable (range) land, other agriculture, and railway rights of way and pipeline.

This is the first complicating factor in the Saskatchewan education property tax system. Many provinces have far fewer classes of property. Alberta has only four categories: residential, non-residential, farmland, and machinery and equipment. Machinery and equipment are not taxed for education funding purposes in Alberta.

In 2009, Saskatchewan created different education mill rates for each category of property. To make things even more complicated, the non-residential category is divided into three brackets based on dollar investment. Each bracket has a separate mill rate.

The mill rates/brackets for each property subcategory for 2009 are:

	2009	2010
Residential Property	**10.08**	**9.51**
Agricultural Property	**7.08**	**3.91**
Non-Residential Property		
Assessed Value from 0-$500,000	**12.25**	**11.85**
Assessed Value from $500,001-$6,000,000	**15.75**	**15.45**
Assessed Value from $6,000,001	**18.55**	**18.28**

This added on even further layer of complexity to the Saskatchewan assessment system.

In contrast, Alberta has two education mill rates for all its property categories:

	2009
Residential and Agricultural Property	**3.39**
Non-Residential Property	**4.98**

A further complexity of the Saskatchewan system is that the assessed value of the property is multiplied by a provincial percentage of value to find the taxable assessment:

Residential	**70%**
Multi-Unit Residential	**70%**
Commercial and Industrial	**100%**
Seasonal Residential	**70%**
Elevators	**75%**
Non-Arable (Range) Land	**40%**
Other Agricultural	**55%**
Railway Rights of Way and Pipeline	**75%**

Alberta doesn't use percentages of value. Every property is taxed at 100 per cent of its assessed value.

The equation to calculate the tax for a property in Saskatchewan is:

Education Property Tax = (Assessed Value of Property x Provincial Percentage) x Mill Rate/1000

The equation for Alberta is:

Education Property Tax = Assessed Value x Mill Rate

On the assessment side, Saskatchewan uses the market value, cost and income approaches.

1) **Market Value Approach:** Also called the sales comparison approach, is based on the theory that market value is directly related to the sale prices of similar properties. This approach works best when similar properties are bought and sold regularly in relatively large volumes.
2) **Cost Approach:** To find the value of the property, the assessor takes the value of the land and adds the replacement cost of any improvements, less accumulated depreciation. The equation used is:
   Total Value of Property = Market Value of Land + (Cost of Improvements - Depreciation)
   This approach is applicable when there are no or limited comparable sales available or when improvements are unique or specialized.

3) **Income Approach:** Also called the rental income approach, this approach only applies to income producing properties

The approach is chosen based on the type of property. Commercial and multi-family properties, for example, are typically assessed with the rental income approach.

In Saskatchewan, property reassessments are done every four years. This means the market value of all land was appraised in 2009 using the base date of June 30, 2006.

In addition to the four-year assessment cycle, owners of income producing properties must provide income and expense information annually.

The four-year reassessment cycle results in significant differences in assessed value versus current market value. At the end of a reassessment cycle, information is seven years out of date, with significant changes in the real market value and the assessed value. This can result in a significant difference in the nominal (based on the assessed value) taxation rate and the effective tax rate (based on the current market value). The effective mill rate values are used in this analysis to allow for more accurate comparison purposes between Alberta and Saskatchewan. In contrast, revaluations are done every year in Alberta. This means that the effective rate in Alberta is the nominal rate.

While not part of this study, Saskatchewan's municipal property taxation system adds another complicating factor. In addition to dealing with the complexities of the provincial property tax system, property owners also face varying municipal mill rate factors.

One of the objectives of recent reforms was to cut and cap school property tax. Good taxation policy should also offer simple and transparent rules. The recent reforms will cut property taxes, at least for residents and farmers. The most recent reform was an effort to seek to encourage new investment growth.

These objectives were addressed by creating a province-wide set of education mill rates (previously, mill rates were set by each local school board). Also, the provincial government is implementing the three-tiered business rate mentioned above.

The result of these reforms in revenue dollar terms can be seen in the table below:

Approximate Education Property Tax by Source (in millions)

	2008	**2009**	**2010**
Agriculture	$105.1	$69.9	$38.6
Commercial	284.6	279.3	273.5
Residential	330.8	273.1	257.7
Grants in Lieu	31.5	26.5	25.9
Total from Taxes	$752.0	$648.8	$595.7
Government Contribution*	782.7	1,104.7	1,156.4
Total Funding for Education	$1,534.7	$1,753.5	$1,752.1

*2008: $0.49x = 752.0 \rightarrow x = 1,534.7$ $y = 1,534.7 - 752.0 = 782.7$
2009: $0.37x = 648.8 \rightarrow x = 1,753.5$ $y = 1,753.5 - 648.8 = 1,104.7$
2010: $0.34x = 595.7 \rightarrow x = 1,752.1$ $y = 1,752.1 - 595.7 = 1,156.4$

The financing of K-12 education policy has been improved since 1905. It is a large step to move to a province-wide set of mill rates. However, when compared with Alberta, one can see there is much that still must be done to improve the education property assessment and taxation system in terms of simplification, competitiveness and timeliness.

3. Framework for the Evaluation of Education Property Tax Policy

To evaluate any tax policy, we must begin with a discussion of basic tax principles. Principles are more basic than policy and objectives, and are meant to govern both[3]. The lack or neglect of principles of taxation by any jurisdiction results in tax systems that are not trusted by taxpayers.[4] The lack of sound taxation principles underlying tax policy also risks tax manipulation and adverse economic impact.

General tax principles include the following:

1) The residents of a jurisdiction ought to contribute towards the support of the government in proportion to their respective benefit (the revenue which they respectively enjoy within the jurisdiction) and capacity (ability to pay).
2) The amount of tax every individual is required to pay should be certain and not arbitrary. The time of payment, the manner of payment, the amount to be paid should be clear and plain to the contributor and to every other person.
3) Every tax should be levied at the time or in the manner that is manageable for the contributor to pay it.
4) Administrative expenses or cost of collecting the tax should not be such that they significantly reduce the actual net amount of revenue for government. If it discourages the contributors, who may now resort to tax avoidance, the administrative burden is high. Taxes should not be much more burdensome to the people than they are beneficial to the jurisdiction.
5) A tax system should not give an undue favourable treatment to some people to the detriment of others. This is because a reduction in taxes for some will increase the taxes of others.
6) A tax should be as broad-based as possible in order to make the tax rate as low as possible for every taxpayer (which in turn reduces tax avoidance and evasion).
7) A tax code must be formulated in simple language so it is easily understood by all who are subject to it. To be able to make long-term individual and business planning possible, it must be a stable, predictable and reliable system that cannot be subject to multiple interpretations and constant change.[5]
8) For a tax to be as simple and clear as possible, it should not have exemptions for some taxpayers. Instead of exemptions, government can adopt some macroeconomic measures such as subsidies and grants as substitutes for exemptions.
9) Where an optimum tax replacement is necessary, it must be phased in incrementally to create as little economic disruption as possible.
10) The optimum tax replacement proposal must be attractive enough for it to be accepted as optimal by all other proponents and promoters of competing tax replacement proposals. The proposed new tax should generate enough revenue to replace the total revenue collected under the tax system that it is meant to replace.[5]

It may not always be possible to achieve all the principles simultaneously. One principle might be given up in order to achieve another. They are, ultimately, general goals which must be balanced by the practical considerations of government tax policy.[6]

4. Evaluation – Education Component of Property Tax under the Current Practice

Saskatchewan Property Tax Rule Attributes	Score
a) Income Equity	**F**
b) Equity Horizontally or Vertically	**F**
c) Vertical Equity	**F**
d) Equity Compared to a True Wealth Tax	**D-**
e) Competitiveness	**D-**
f) Simplicity/Administrative	**D-**
g) Transparency	**D**

a) Income Equity : F score

The education property tax in Saskatchewan rates poorly in terms of income equity, in other words from the perspective of the taxpayer's ability to pay. This is because property tax rates are not directly based on the income generated by the properties.[7]

b) Horizontal Equity: F score

The horizontal equity property tax principle policy, in general terms, states that properties of equivalent value should pay equivalent tax.[8] There is extensive research to demonstrate that commercial and industrial property receive no greater benefit from municipal services than residential property. While this contention is disputed by some in terms of certain kinds of municipal services, it is certainly true for public education. On this basis, no mill rate differential can be justified between any category of assessed property.

i) The Effect of Income Tax Deductibility on Equity

The residential property owner pays his property tax out of his after-income-tax income. On the other hand, business or farm property taxes are deductible under the income tax and so education property taxes are paid from pre-income-tax income. The savings in income tax that the business makes partly offsets the tax burden for the business, but it also creates an inequity between the two types of taxpayers.

For example, assume an average corporate income tax rate of 30 per cent. If a business has a property taxed at the same rate as the homeowner, both paying property tax of $1,000, while the $1,000 is the real property tax paid by the homeowner, the real amount paid by the business would be less:

Property tax liability	$1,000
Reduction in corporate income tax liability (30% of $1,000)	(300)
Net cost to the business of the property tax	$700

To achieve the horizontal equity principle, business property taxes could be levied at a slightly higher rate than residential property taxes to offset their income tax deductibility. The

Saskatchewan property system tax recognizes this by taxing most non-residential properties at 100 per cent of assessed value, but taxing residential properties at 70 per cent of assessed value. However, by focusing the adjustment on the assessed value rather than on the tax rate, this approach is flawed and creates further inequities (e.g. rental residential property).

Under current rules, for a residential property in Saskatchewan to pay a $1,000 property tax bill, the property would have to be assessed at $150,217.81 to derive a taxable assessment of $105,152.47 with a mill rate of 9.51 for 2010 or $1,000. A non-residential property assessed at $150,217.81 would pay $1,780.08 in property tax before income tax deductions of 30 per cent or $1,246.56 in after-income-tax education property tax. The actual property tax paid by the homeowner is approximately 56 per cent of the amount of property tax paid by the business property.

To make both properties pay an equal after-income-tax property tax, the business could pay an effective property tax rate 1.43 times the rate of the residential property.

Using this differential factor, if the residential education property tax rate (assessed value x 70% x 0.951%) is 0.67 per cent (or 6.7 mills), the business property tax rate should be taxed at 0.951 per cent of market value or 9.51 mills. This analysis only partially justifies mill rate differentials from a tax policy perspective as explained below.

ii) Other challenges to tax equity

- Residential property that is rented out is not treated as a revenue-generating business property but is taxed as personal residential property for administrative ease and potential future change in use.

- Owner-occupied residential property is generally exempt from capital gains tax while non-residential property is not exempt.

- Farmland in Saskatchewan is taxed at a level that may be competitive in 2010 with Alberta but it is not taxed at a level that treats this property type as comparable to any other type of real property in Saskatchewan.

iii) Limitations for Small Business

Although the model presented above works in general terms for business properties, it does not always work for small businesses which have a lower business income tax rate. What the small business gains through lower corporate tax, it partially loses through lower property tax deduction in corporate tax calculation.

For example, if we assume an average small business tax rate of 15.5 per cent:

Property tax liability (150,217 x 0.01185%)		$1,780.08
Reduction in corporate tax liability	(15.5% of $1,780.08)	(275.91)
Net cost to the small business		$1,504.16

(0.01185% is the 2010 mill rate for non-residential properties assessed below $500,000)

The net cost to the small business of the property tax of $1,504.16 is higher than that of the general, manufacturing and processing business or the residential property. The education tax mill rate which the government is applying to lower valued property for the small business is being taken back through a still-too-high education property tax mill rate. Once again, the horizontal equity principle is violated.

Even though the income tax deductibility of non-residential properties may justify higher property tax rates for businesses, governments must still be watchful over the differences between residential and business property mill rates. "The relative heavy property tax burden for small businesses conflicts with other tax policy objectives. The reduced income tax rate for small business is intended to foster investment in new and small businesses, create employment, encourage innovation and ensure some progressivity in the corporate income tax. The [education] property tax [system] works against those objectives."[7] This is true even with the complexities of the tiered mill rates for non-residential property.

iv) Comparison to Alberta

In contrast, Alberta achieves a much better level of horizontal equity among types of property. The 2009 education property tax mill rate in Alberta is 3.39 on residential and agricultural properties' fully assessed values. Business property is taxed at 4.98 mills of fully assessed value. The mill rate differential suggests that non-residential properties pay a 46.9 per cent premium to residential property which very roughly offsets the income tax deductibility of property taxes attributed to non-residential property taxes.

Commercial mill rates in Alberta remain the same for all assessed values of property regardless of size. Saskatchewan has three tiers, which does little to address equity issues but adds complexity and hinders transparency. The scale of real estate investment doesn't fully measure wealth-generating capacity.

c) Vertical Equity: F score

Vertical equity is the concept of fairness used to justify progressive tax systems: that those who earn more or have more wealth should be taxed at a higher rate because they have a greater ability to pay.

Leaving aside the discussion of whether a progressive system is fair, property tax assessment is not equitable by the standards of progressive tax systems because real property is not a directly correlated measure of income or wealth.[8]

In Saskatchewan, there are five different education property mill rates charged on assessed values of properties, according to their use and assessed values. The mill rates for residential properties and agricultural or farm business do not increase progressively. In the case of commercial/business properties, there are three levels of mill rates charged, depending on the assessed value of the property.

* $0-$500,000 - 12.250 mills
* $500,001-$6,000,000 - 15.750 mills
* $6,000,000+ - 18.550 mills

This system incorrectly assumes that overall assessed property value either measures ability to pay or (as described above) correctly offsets varying income tax rates.

By imposing higher taxes without consideration of the taxpayer's ability to pay, the Saskatchewan system discourages investors from increasing their investment in Saskatchewan.

Across Canada and around the world, there is a trend for provinces and cities to drop progressive tax rate systems in order to avoid discouraging investment. Such an approach would be more consistent with the often-stated growth agenda for Saskatchewan.

On the grounds of equity, even if assessed value of property is used instead of income, it is difficult to justify a difference in residential and non-residential effective education property tax rates of more than a factor of 1.43 to 1.45. There is a strong argument that the differences in mill rates between farmland, residential and non-residential property should be narrowed. A corporate tax rate of 31 per cent produces a differential factor of 1.45 which implies that if the residential effective education property rate is 6.67 mills (9.51 mill rate in 2010 times the 70 per cent taxable assessment inclusion rate for residential property), a non-residential education mill rate of 9.51 in 2010 is reasonable when equity principles are taken into consideration.

d) Equity Compared to a True Wealth Tax: D - score

Using the same tax fairness principle to evaluate the education component of property tax as a wealth tax, it scores a D-.

A true wealth tax is based on net wealth or net worth (assets minus liabilities).[9] If property tax is based on the difference between the property value and the liability attached to that property (such as interest on the mortgage and the mortgage itself) then it would qualify as a net wealth/worth tax[10] – but this is not the way property tax is administered in Saskatchewan.

Property taxes are used extensively and are therefore generally accepted as an acceptable means of generating government revenue, in spite of their inherent flaws. Property taxes are also theoretically hard to avoid. In fact, the only way to avoid a property tax in a jurisdiction is not to invest in that jurisdiction. Because of the discriminatory nature and distortional potential of property tax, this form of taxation must be applied at low rates because of the inherent shortcomings against the accepted measures of some taxation policy.

Because this form of taxation can do much to distort or discourage investment, any jurisdiction seeking investment will need to keep property taxes low.

The currently applied levels of education property taxes in Saskatchewan on non-residential property will encourage tax avoidance through non-investment because the investment alternatives (i.e. Alberta) are quite easy.

e) Competitiveness: D score

Competitiveness -- the relative ability of a jurisdiction to attract and retain investments and career opportunities for its citizens – is poorly served by the Saskatchewan property tax system.

A rational investor prudently studies the investment climate in a jurisdiction and compares the jurisdiction with others before making a decision. The decision is driven or motivated mostly by profitability and risk. What happens to the next dollar of investment matters a lot to the investor. An investor will prefer the jurisdiction with a tax policy that is not punitive or does not heavily tax the next dollar of investment. Obviously, a tax policy that puts higher taxes on higher levels of investment discourages further investment.

In Saskatchewan, if a business wants to expand to increase production, it will likely pay a higher property tax rate. For instance, if the property expansion rises from $500,000 to above $6,000,000, the education property tax mill rate rises from 12.25 to 18.55. If this investment decision was made in Alberta, a commercial mill rate of 4.98 would have been charged on this property regardless of the size of the expansion.

From the KPMG *Competitive Alternatives* study (2008)[11], which is a guide for comparing business locations in North America, Europe and Asia Pacific, businesses making location choices for capital investment may be discouraged by Saskatchewan's high and complex education property tax. The analysis of this study shows that even a small percentage difference can translate into a large amount of money on a big investment. For instance, for a $10 billion power plant investment, the difference could be as high as $135,681,450 on a nominal basis per year between Saskatchewan and Alberta (see appendix 7).

f) Simplicity/Administrative: D score

The attribute of simplicity as a tax policy principle requires that taxpayers be easily able to understand the rules and comply with them correctly without incurring undue costs. Simplicity is important, not only to the taxpayers but also to the tax administrators. Complex tax rules lead to errors and cause taxpayers to distrust the system.

In general terms, education property tax is simple compared to other forms of tax. However, when we compare the education property tax rules in Saskatchewan to those of Alberta, this is not the case. Alberta has a single mill rate (4.98 mills) for all commercial properties while Saskatchewan has three different rates for properties of different values (see above.)

The complexity of Saskatchewan's property tax system is worsened by the different percentages of value for different property classes and the time lag in valuation described in the following section. This makes the calculation of the effective education property tax rate more complex in Saskatchewan than almost all other jurisdictions, including Alberta.

g) Transparency: D score

Transparency requires that the taxpayer should know that a tax exists, and how and when it is due to be paid. Where there is transparency, the taxpayer knows the actual cost of a transaction, the total tax liability and to whom the tax is paid. Without transparency, the taxpayer will not know how the tax affects him. When taxpayers see that a tax is applied equitably and understand how it is determined and how it is used, they are more likely to see it as a responsibility and not a forceful and arbitrary imposition.

The Saskatchewan education property tax does not fully satisfy this requirement. The reassessment of property in Saskatchewan is done every four years and valued at a date three years prior to the reassessment year.

In Alberta, it is done every year. The yearly assessment makes it easier for taxpayers to remember to prepare for the change in tax burden that may arise from the reassessment, and the changes in tax burden will typically be smaller and more incremental.

By reassessing every four years – which can create a lag time as long as seven years because of the three-year lag in assessed values at the outset of the reassessment year – the Saskatchewan system hits taxpayers with a sudden, large and much more burdensome increase in taxes that aggravates the uncompetitively high taxation rate. This further encourages avoidance through non-investment.

The comparison to Alberta also hurts the credibility of Saskatchewan's taxes. Since property taxpayers can see that Alberta's education system functions with a much lower and less confusing mill rate structure, they start to lose confidence in the Saskatchewan government's reasons for levying the tax and therefore avoid paying the tax through non-investment.

Low Rate Needed because of the Narrow Base

Education property tax rules in Saskatchewan continue to have significant shortcomings which imbed a disincentive to invest in real estate in Saskatchewan. Jurisdictions that offer lower education property tax rates benefit from more non-residential investment.

Taking undue advantage of real property because of its immovability contradicts one of the principles of a good tax system, which demands that the tax base[12] should be as broad as possible so that the tax avoidance pressure will be less. Where the bulk of the tax burden is placed on a narrow tax base, tax avoidance and evasion tactics are promoted. In this case the only means to avoid this tax is to not invest. This narrowly defined capital has a narrow base. This means that the rate of property tax must be very low to limit avoidance. This also means that only a limited number of public services should depend on it.

Comparing with Corporate Capital Tax

The Saskatchewan government, over successive administrations, is eliminating or reducing capital taxes. An example of this is the reduction and elimination of the corporate capital tax rate between July 1, 2006 and July 1, 2008. "As a result of the April 6, 2006 Saskatchewan Budget, the corporation capital tax rate used by corporations to calculate their corporation capital tax payable, was reduced effective July 1, 2006 and completely eliminated on July 1, 2008. Also, the corporation capital tax resource surcharge rate paid by a resource corporation was reduced July 1, 2006."[12]

This was done to encourage business investment in Saskatchewan and has been shown to have the desired effect of prompting business investment in Saskatchewan after 2006. The result was a faster growing base and additional government revenue.

According to a submission to the Saskatchewan Business Tax Review Committee in summer 2005 by the Saskatchewan Real Estate Association, "Property is capital; taxing it subtracts from our economic base. Every year, property owners must pay a percentage of their asset's value to the government. Except in rare cases, the amount has nothing to do with income (for residential property). It is a deduction from the tax-paid asset that represents a shriveling of the capital base every economy needs to grow . . . The present structure is a leftover from the early days of the last century when most families lived on farms and the most widelyheld resource was land. It harkens back to the times before the income tax, sales tax, gas tax or resource revenues. A tax on property is not suited to services to people, who are highly mobile today, and need the best possible education. It is time to reform our school finances.

"The property tax system is overgrown with complex assessment rules, tax factors, asset classes, and mill rates. It is sustained by an expensive bureaucracy whose workings are obscure. Very few if any really understand the system. It lacks transparency and is badly in need of a thorough overhaul . . . Education takes over half the revenue raised from property taxes. The Boughen Commission showed that this level is the highest in Canada. In recent years, Saskatchewan has reduced several major taxes at the provincial level. We have recognized the negative impact the corporate capital tax has on investment. But the province has largely ignored the tax on business investment capital that is represented by property. This tax consumes value that we need to finance development . . . Property in Saskatchewan was taxed for $1,252,439,850 in 2004. Of that amount, $439,790,896 was exacted from commercial and industrial property. Property taxes are a greater cost to business than even the corporate capital tax. They rank third overall in magnitude province wide, exceeded only by the taxes on personal income and sales."[13]

Summary

Depending upon non-residential property rates to any large extent is poor taxation policy because of the inherently narrow base of property taxation.
From this analysis, an evaluation of the newly introduced education property tax rules as applied in Saskatchewan can be summarized as follows:

- They fail the test of both vertical and horizontal equity.

- They fail the test of the benefit-based principle.
- They are not at a competitive rate of taxation compared to Alberta.

5. Marginal Effective Tax and Economic Impact

Introduction

This project focuses only on the education portion of the property tax on commercial property. It is not a tax related directly to the benefit received by the property owner or property user. As such, it may have a different impact on the economy and behaviour than a local government tax on commercial property or on residential property.

We have concluded that the characteristics of this tax are closest to a broadly imposed corporate capital tax. Whereas a corporate capital tax is imposed on the capital or funds of a commercial organization, the education tax is imposed on the actual assets of that organization. In those few places that still have both taxes, they have the effect of double taxation.

In this section of the report we will discuss the impact of this tax on marginal effective tax rates (METR), the economy and the behaviour of business persons and investors.

Marginal Effective Tax Rate

Appendix D of the 2005 Saskatchewan Business Tax Review Committee report dealt extensively with the concept of METR. Briefly, the METR attempts to measure the additional rate of return on a capital investment that a business will require in order to pay the corporate taxes that will arise as a result of that investment.

For example, let's say that business owners require a 12 per cent after-tax return in order to justify a particular level of investment risk. If it is determined that, in order to meet that requirement, a before-tax rate of return of 20 per cent is required, then the METR is 40 per cent, according to this formula:

$$\mathbf{METR = (20\%-12\%)/20\%}$$

The federal Department of Finance, the C.D. Howe Institute and Professor Ken McKenzie, University of Calgary, have all been involved in the development and use of this important tool. They have not included property tax on commercial property in their analysis, for two reasons. First, in the analysts' view, local taxes represent a fee for service and are not actually a tax; second, there is such great variation in the levels and implementation of property tax across Canada that meaningful comparison is, in their view, impossible.

Since this report is limited to the proportion of property tax for education levied on commercial property, the first reason does not apply. The second reason is more difficult to deal with; however, by limiting our METR comparison to Alberta we have been able to get reliable data to make the necessary calculations.

The Calculation

We started with the METR calculation for Saskatchewan and Alberta for 2008 and determined the corporate taxes that were included in that calculation. To determine the impact of the education portion of property tax, we added the amount that will be collected from commercial property in each jurisdiction to the total determined. This gave us enough information to make the following calculation:

	Saskatchewan	Alberta
METR – excluding Property taxes	**28.60**	**22.00**
METR – including the Education portion of Property tax	**33.33**	**24.20**

(Using effective rates of education property tax of 1.12 per cent and .50 per cent for Saskatchewan and Alberta respectively)

To illustrate the importance of these differences, before considering the property tax and sticking with our required after-tax return of 12 per cent, a Saskatchewan firm would have to earn a before-tax return of 17 per cent and an Alberta firm a return of approximately 15.4 per cent.

If the education portion of property tax is included, the Saskatchewan firm would have to have a before-tax rate of return of 18.3 per cent and the Alberta firm a before-tax rate of return of 15.8 per cent. This difference in before-tax rate of return is significant enough to influence location decisions. On a $5 million project, the Saskatchewan location would require an additional $125,000 of before-tax income.

The recent changes in Saskatchewan property tax, which dropped the education funding portion from $284.6 million in 2008 to $279.3 million, had only a small positive impact on the METR for Saskatchewan.

Economic Impact

The education portion of property tax on commercial property has the same attributes as a corporate capital tax – the most important being that it increases the cost of ownership and this cost is imposed whether or not a firm is profitable or has cash flow to meet it.

Much of the summary evidence presented here is taken from the report of the 2005 Business Tax Review Committee. In turn, this report used information and data provided by the Saskatchewan Ministry of Finance, Department of Finance Canada and the C.D. Howe Institute. It is important to remember that the data pertains to corporate capital taxes and not to the education portion of property tax on commercial property. We have made the link to corporate capital taxes based on our understanding of both taxes.

Most economists conclude that corporate capital taxes have a negative effect on the economy, worse than corporate income taxes or taxes on wages. In 2008, the Organization for Economic Co-operation and Development (OECD) made the following observation:

"One priority should be to broaden the business tax base and lower tax rates on capital further. Marginal effective tax rates on business investment have been cut sharply in recent budgets: the federal corporate rate is being reduced by a third and the federal capital tax (an inefficient tax on wealth) eliminated. Most provinces are also phasing out their capital taxes, in part in response to federal incentives. But more could still be done. Businesses in some provinces pay retail sales taxes on inputs, penalizing investment."

In a 2007 e-Brief published by C.D. Howe Institute:

Still a Wallflower: The 2008 Report on Canada's International Tax Competitiveness
By Duanjie Chen and Jack Mintz

"Domestic investment depends on after-tax returns, as compared to what can be achieved by investors in other parts of the world. If a business earns a higher return on capital in a particular jurisdiction, it will expand its investment in that jurisdiction. Corporate income tax, sales tax on capital inputs, and other capital related taxes reduce the after-tax return on investment, which affects the demand for capital by business. Higher tax on business investment will cause capital investment to decline in a jurisdiction, thereby impairing economic growth. A 1 percentage point increase in the effective tax rate on capital investment reduces investment in plant, equipment and non-residential structures by 0.5 to 1.0 percentage points (Mintz 2007). The effect of taxes on mobile foreign direct investment flows is even stronger, with a percentage point increase in the effective tax rate leading to a 3 percentage point decline in capital inflows."

In 1997, the Saskatoon Chamber of Commerce engaged two economists, Don Gilchrist and Larry St. Louis from the University of Saskatchewan, to consider the effect of property taxes (not limited to education portion) on investment patterns in Saskatoon. The resulting report is one of the few that pertains to this particular tax.

The key finding of the Gilchrist/St. Louis study was that, as a business community, Saskatoon had underestimated the adverse impact of uncompetitive property taxes on investment decisions, and that these impacts were most directly felt by small businesses.

The authors concluded:

"The weight of the empirical evidence supports the conclusion that taxes have significant effects on new business location and new investment. This is consistent with general perceptions and with a broad range of public policies designed to attract and retain productive economic activity in communities, provinces and states, and countries."

In a 1997 report to the City of Saskatoon, a tax review committee concluded that the substantial surtax on commercial property (that is where the effective rate is higher than the rate on residential property) is not fair or equitable and that it has the potential to adversely affect economic development.

"Although the evidence indicates that most local government jurisdictions in Canada impose a similar surtax (and, in fact, the differential is higher in some other jurisdictions), we are unable to recommend the continuation of the current differential."

We are certain that the same conclusion would be drawn from an analysis of the education component of that tax on commercial property.

Taxes and location decisions are closely tied. The KPMG analysis section of this report mimics the kind of decision analysis that a business might undertake in order to decide on the location of a project.

The "Wealth Effect" section of this report provides both anecdotal illustrations of the impact of property taxation on investment decisions and measures the macro impact on investment in Saskatchewan.

6. Impact on Cash Flows and Investment Decisions

The data for the tax comparison appendices was adapted from the KPMG *Competitive Alternatives* study (2008). It is a "guide for comparing business locations in North America, Europe and Asia Pacific."[11] The study measures 27 business cost components as well as many non-cost factors to competitiveness. It spans 10 countries (Australia, Canada, France, Germany, Italy, Japan, Mexico, the Netherlands, the United Kingdom and the United States) and 17 industries. The analysis is based on cost information from between July 2007 and January 2008. To learn more, please visit the KPMG *Competitive Alternatives* website (www.competitivealternatives.com).

The jurisdictions in the contained analysis were chosen because many of them are of a comparable size and are feasible location alternatives. Also, many of them have a similar economic climate and outlook. Potential investors in some of the cities are looking at investing in similar industries or are already involved in those industries in another jurisdiction. The industries were chosen because they were representative of potential or present industries in Saskatchewan and Alberta.

The effective tax rate for the education portion of property tax is the rate the taxpayer will be paying after the mill rate and provincial percentage have been applied, compared to the current market value. That is:

Effective Tax Rate = Taxes Paid/Current Market Value

The difference between this effective rate and the nominal rate is that the effective rate is based on estimates of current market values while the nominal rate is calculated using the base year assessment (in this case, the base year is 2006). The estimates of current market value were determined in this report by a review of market value changes between June 2006 (the assessment valuation date in Saskatchewan applied in the 2009 Saskatchewan reassessment) and June 2009. We determined this valuation through discussions with appraisal firms in Regina and Saskatoon and commercial real estate firms in Regina and Saskatoon. These values are estimated in this report to adjust the effective value of property by 30 per cent from June 2006 to June 2009. This result is a substantial difference between the nominal mill rate (higher) and effective mill rate (lower).

Nominal Tax Rate = Taxes Paid/Assessed Value

Looking at appendix 5 and the summary table below, one can see that, in every industry, Saskatchewan's effective tax rates are larger than Alberta's and the nominal rates are much higher.

One of Saskatchewan's objectives in education property tax reform was to encourage growth and investment in the province. The KPMG analysis shows that a property investment in Saskatchewan or for a similar plant in Alberta would result in a nominal cost disadvantage in Saskatchewan ranging from a low of $25,352 per year to a high of $124,723 per year and an effective cost disadvantage ranging from a low of $14,278 per year to a high of $73,052 per year.

Expansions are even more adversely affected because of the stepped commercial mill rates in Saskatchewan. If the KPMG investment samples (found in appendix 7 are expanded (doubled), then the nominal cost disadvantage rises to a range of $52,708 per year low and to a high of $258,834 per year, and the effective cost disadvantage rises to a range of $30,305 per year low and a high of $155,493 per year.

These property tax load differences discourage business owners from building plants in Saskatchewan. For example, the cost disadvantage for a $1.9 billion oil upgrader built in Saskatchewan rather than Alberta is $25,764,450 per year nominally and $16,626,857 per year effectively. For a $4 billion polygeneration power plant, the disadvantage is $54,261,450 per year nominally and $35,024,413 per year effectively.

Even a small percentage difference can be quite high in terms of a dollar difference on a large investment. The difference could be as high as $135,681,450 per year nominally or $87,588,857 effectively per year between Saskatchewan and Alberta for a $10 billion power plant. While the report uses effective tax rates in calculating the difference in the METR, the reader should be cautioned that only the most sophisticated and well acquainted investor could discern the difference between nominal and effective mill rates. Many potential investors would simply compare Saskatchewan's top nominal education mill rate of 18.55 mills to Alberta's 4.98 mills.

The second summary table, which can also be found in appendix 8, illustrates an investment decision on whether to expand (double in size) in Saskatoon or build new in Red Deer, based on differences in education property taxes alone. The calculations are based on 2008 numbers from the KPMG *Competitive Alternatives* study. The decision is broken down by industry. Both nominal and effective amounts were examined. One can see by looking at the table that, in every investment decision, Red Deer would be chosen if the decision was based solely on education property tax differences. This means Saskatchewan is overwhelmingly uncompetitive in the area of education property taxes in every industry compared to Alberta.

Average Education Property Tax Amounts and Effective Tax Rates by Province for Each Industry

Industry	Saskatchewan				Alberta			
	Nominal $ Amount	**Nominal Tax Rate**	**Effective $ Amount**	**Effective Tax Rate**	**Nominal $ Amount**	**Nominal Tax Rate**	**Effective $ Amount**	**Effective Tax Rate**
Overall Industry Average	58,261	1.53%	$42,703	1.12%	$21,476	0.50%	$21,476	0.50%
Manufacturing Average	102,902	1.57%	78,158	1.19%	36,818	0.50%	36,818	0.50%
Aerospace	106,356	1.58%	76,703	1.14%	37,694	0.50%	37,694	0.50%
Agri-Food	69,444	1.54%	50,986	1.13%	26,021	0.50%	26,021	0.50%
Automotive	143,582	1.64%	102,172	1.17%	48,556	0.50%	48,556	0.50%
Chemicals	69,444	1.54%	50,986	1.13%	26,021	0.50%	26,021	0.50%
Electronics	185,332	1.72%	133,661	1.24%	60,609	0.50%	60,609	0.50%
Metal Components	138,332	1.63%	98,157	1.16%	46,762	0.50%	46,762	0.50%
Pharmaceuticals	94,349	1.56%	68,740	1.14%	33,889	0.50%	33,889	0.50%
Precision Manufacturing	40,964	1.51%	29,890	1.10%	15,612	0.50%	15,612	0.50%
Telecommunications	83,941	1.55%	61,536	1.13%	31,225	0.50%	31,225	0.50%
Plastics	143,350	1.64%	101,766	1.16%	48,807	0.50%	48,807	0.50%

For more details on Saskatchewan and Alberta's property tax values by industry and their impact on overall cash flows, please refer to the appendices.

Investment Decision: Expand (Double) in Saskatoon or Build New in Red Deer?

Industry	Investment Amount	Saskatoon		Red Deer		Difference		Decision
		Nominal	Effective	Nominal	Effective	Nominal	Effective	
Overall Industry Average	$4,497,000	$79,211	$54,319	$22,395	$22,395	$56,816	$31,924	**Red Deer**
Manufacturing Average	7,708,000	142,984	105,100	38,386	38,386	104,598	66,714	**Red Deer**
Aerospace	8,013,000	148,641	109,924	39,905	39,905	108,736	70,019	**Red Deer**
Agri-Food	5,304,000	96,440	95,937	26,414	26,414	70,026	69,523	**Red Deer**
Automotive	10,258,000	190,286	140,952	51,085	51,085	139,201	89,867	**Red Deer**
Chemicals	5,304,000	96,440	67,082	26,414	26,414	70,026	40,668	**Red Deer**
Electronics	12,941,000	230,894	168,658	64,446	64,446	166,448	104,212	**Red Deer**
Metal Components	9,846,000	182,644	135,292	49,033	49,033	133,611	86,259	**Red Deer**
Pharmaceuticals	7,025,000	130,314	94,299	34,985	34,985	95,329	59,314	**Red Deer**
Precision Manufacturing	3,182,000	51,135	37,124	15,846	15,846	35,289	21,278	**Red Deer**
Telecommunications	6,365,000	118,071	83,862	31,698	31,698	86,373	52,164	**Red Deer**
Plastics	10,358,000	192,141	142,326	51,583	51,583	140,558	90,743	**Red Deer**

7. Behavioural Responses to Changes in Taxes or Similar Charges

Changes in tax rates and the mix of taxation in Saskatchewan over the past 15 years have provided economists, public policy think tanks and citizens with a great deal of data to analyze. In this section, we look at some anecdotal examples of the positive effect tax changes have had on investment, income and commercial activity in Saskatoon and Saskatchewan.

City of Saskatoon

In 2001, on the basis of the recommendation of the 1997 Tax Review Committee, the City of Saskatoon started a 10-year process of changing the allocation of taxes among property classifications. When fully implemented, this policy change will limit the effective tax rate on commercial property to 1.75 times the residential effective rate. (At the time of that report, commercial property was 2.11 times the residential effective rate.)

Since the implementation of this approach in Saskatoon, the city's per capita non-residential assessment has grown much faster than that of the rest of the province. The per capita non-residential assessment has grown from 43.20 per cent of Red Deer's non-residential assessment per capita in 1997 to 67.30 per cent of Red Deer's in 2009, reflecting an investment behavioural change in Saskatoon.

Province of Saskatchewan

There are four illustrations that result from changes in the tax or similar charges regimes since 1995. All of these illustrations are taken from the 2005 report of the Business Tax Review Committee (see pages 81-83 and appendix G):

In 1995, the province reformed the tax structure for the manufacturing and processing (M&P) sector by lowering the corporate income tax rate and by exempting that sector from provincial sales tax on certain inputs and capital acquisitions. Since then, the growth in value of Saskatchewan's M&P shipments has exceeded the national average. Between 1994 and 2004, the growth in Saskatchewan was 125 per cent compared to the Canadian average of 71 per cent.

In 2002, the province introduced a broad-based reform of its royalty and tax regime for the energy sector. These changes included a reduction in the corporate capital tax resource surcharge on new production. From 1999 to 2005, employment in that sector increased from approximately 17,000 to 25,000. Admittedly, strong international prices are a major contributor to this growth; however, the framework was in place to attract exploration activity.

In 2000, the province lowered personal income tax rates significantly. Since then, the number of higher income earners paying tax in the province has increased. In 1999, only 2.1 per cent of all taxpayers earned in excess of $100,000; by 2003, that percentage had increased to 3.1 per cent. The initial revenue loss (over $400 million) was recovered through economic growth before the end of the phase-in period of 2003-2004.

(In fairness, it should be noted that this last example has less to do with investment behaviour and more to do with tax avoidance behaviour. It is likely not the case that there were more people earning over $100,000 by 2004; rather, it is more likely that people in this tax bracket made less effort to try to avoid paying income tax. As such, this example doesn't compare directly to property tax, since the only way to avoid paying property tax is not to invest in property.)

In October 2005, the Saskatchewan Business Tax Review Committee asked C.D. Howe Institute to estimate the net cost of changes in the corporate income tax regime. The net cost determination took into account taxes previously paid to another jurisdiction that would be paid to Saskatchewan under a lower corporate income tax regime. The study is reproduced in appendix G of the 2005 Saskatchewan Business Tax Review Committee report.

The study concluded that the corporate tax base in Saskatchewan would expand by 11 per cent if the province implemented a five-point corporate income tax reduction If income shifting was not considered, C.D. Howe Institute estimated that revenue lost from the corporate tax rate changes would be approximately 23 per cent. When shifting was considered, the revenue loss would be between 11.5 per cent and 15 cent. Income shifting in the C.D. Howe report refers to corporate investment and accounting adjustments made to operating income in various provincial and international jurisdictions in order to minimize tax costs for businesses.

Conclusion

Taxes influence behaviour and different taxes influence behaviour in different ways. Evidence from economic modelling suggests that corporate capital taxes have adverse effects on investment.

Fiscal policy studies have always told us that the main reason for taxation is to raise money for government expenditures. However, taxation can also influence behaviour that is consistent with government goals.

8. The Wealth Effect

In this section, we examine a means to make education property tax rates even more competitive in the future -- the path to a virtuous cycle of generating economic growth. The examples of investor behaviour used in this section are based on actual outcomes in Alberta and Saskatchewan.

For several consecutive years, including this year, the Regina & District Chamber of Commerce and the Greater Saskatoon Chamber of Commerce have sought and achieved support for the resolution at the annual Saskatchewan Chamber of Commerce policy resolution meeting to request certain improvements to the assessment and taxation system in Saskatchewan from the Government of Saskatchewan. These include:

1. A more frequent reassessment cycle to improve assessment accuracy.
2. Setting all property taxable assessment at 100 per cent of assessed value to improve transparency while still providing for differing mill rates for the various property categories but doing so in a transparent fashion.
3. Capping the effective tax rate for non-residential assessment at 1.75 of the residential effective tax rate (as is the case in Saskatoon).

The following analysis demonstrates the beneficial impact of these policies, using the City of Saskatoon versus the City of Red Deer as an illustration of the real-world investment impact of this policy framework.

When the Greater Saskatoon Chamber of Commerce started its research on property taxes in Saskatchewan through the Gilchrist/St. Louis study, the fundamental question was, “Do property tax levels affect business investment decisions?” That independent study’s findings were: “Property tax levels do materially and directly affect investment decisions.” In short, the higher the non-residential tax rate, the lower the non-residential investment levels.

Our Chambers contend that Saskatchewan should seek greater levels of non-residential property investment. The public policy importance of non-residential property investment begins with the fact that these investments are the foundation upon which the indigenous tax base is built and from which all future property tax revenues will be derived. Most future provincial sales and income taxes from both business interests and residents will be considerably dependent upon sustained and growing non-residential real property investment in Saskatchewan. The benefits of a competitive and principle-based education property tax policy extend far beyond the public interests of tax revenue in that a sound economic base for a jurisdiction needs growing investment in real property in the jurisdiction; and upon that base, the livelihood of its citizens depend.

A review of the comparative non-residential tax base of Alberta and Saskatchewan shows that the non-residential assessment base in Saskatchewan is substantially smaller on a per capita basis than in the Alberta comparative. These differences in the non-residential tax base have occurred despite the very similar attributes of the resource bases of the two provinces. In fact, our Chambers contend that the diversity and strength of the resource base of Saskatchewan is superior to that of Alberta from a diversity and relative wealth perspective, particularly on a per capita basis. The 2009 non-residential assessment base is approximately $129 billion in Alberta compared to $18 billion in Saskatchewan. The non-residential per capita assessment base of Alberta is over $35,500; in Saskatchewan, it is under $18,000. This stark contrast is a sobering testament to the chronic business property tax avoidance evident in Saskatchewan.

While it would be incorrect to attribute all of this to property taxation differences, they are definitely part of the cause.

Comparing the per capita non-residential assessment of Red Deer to Saskatoon, Red Deer's $25,451 versus $13,255 (nominal) in Saskatoon. Red Deer's non-residential property assessment base is nearly twice that of Saskatoon. Red Deer's base is between three and four times the comparative non-residential per capita assessment bases in Moose Jaw and Prince Albert. Similar gaps are shown when comparing non-residential building permits issued in Saskatoon and Regina to Calgary and Edmonton.

A March 2009 Canada West Foundation report, "Economic Development Issues of the Four Western Provinces to 2020," examines future planned major investment projects in Alberta and Saskatchewan. These results, likewise, are consistent with the current differences between the two provinces.

If Saskatchewan were, over time, to match Alberta's non-residential per capita property assessment base, Saskatchewan could generate more property tax revenue and have a much sounder economic base. A bigger tax base means lower tax rates for the same level of public expenditure.

Using the Red Deer to Saskatoon comparative as a baseline for potential incremental non-residential investment potential of the province, Saskatchewan could reduce its non-residential education mill rate by 53 per cent from 2010 levels and still generate the same $273 million in property for provincial education purposes currently expected to be raised from this category of property if the per capita non-residential assessment in Saskatchewan were to grow to Red Deer's level.

With a properly structured and competitive education property tax policy and some adjustments to province-wide municipal tax policy, the accelerated growth in Saskatchewan's non-residential assessment base would be enough to bring non-residential education mill rates in Saskatchewan to levels competitive with those in Alberta. This growth in non-residential assessment per capita applied to province-wide municipal taxation could also result in significant further declines in municipal portions of residential and farmland mill rates, thus further improving Saskatchewan's aggregate competitive position.

This analysis also infers that Saskatchewan could attract many billions of dollars -- perhaps even $100 billion - in new non-residential property investment, along with the spin-off benefits stimulated by this investment level. At even a modest mill rate of 10, an additional $100 billion in non-residential assessment in Saskatchewan could result in $1 billion in incremental annual municipal property tax revenue that could be invested in infrastructure, community services or lower taxes for all categories of taxpayers.

Growth in investment of this scale is possible in Saskatchewan, but changes to the current education property tax mill rates will be required to improve this province's prospects to attract this scale of investment.

Appendix 4 illustrates a growth scenario that would allow Saskatchewan to grow its assessment base and be property tax competitive while growing revenues for government.

Growing the Saskatchewan per capita non-residential assessment base by 214 per cent would offer substantial province-wide benefits over and above the potential 53 per cent decline in non-residential education mill rates. The province's ability to better attract, retain and employ young people, including Aboriginal youth, could be dramatically improved just by new construction jobs.

If a 15.10 average non-residential education mill rate in Saskatchewan in 2010 generated $273 million in tax revenue with the current Saskatchewan non-residential assessment base, a nominal non-residential mill rate of 7.47 mills could generate the same $273 million in education property taxes if the non-residential assessment base in Saskatchewan achieved Alberta's per capita levels. This level would be much more competitive with the Alberta 2009 mill rate of 4.98 mills.

However, Saskatchewan also needs to be aware that Alberta has lowered its non-residential education mill rate in each and every of the last 17 years. Being competitive is a moving target.

The province-wide non-residential investment growth described above would not occur instantaneously, but could occur surprisingly quickly. This growth results in even more government revenue at a lower tax rate on a lower tax base. The Saskatoon experience illustrates this phenomenon.

The provincial and federal government revenue streams from sales and income taxes would also grow as a result of economic multipliers from accelerated investment activity. At the same time, this economic growth would increase career choices for our citizens.

This wealth effect, derived from a properly structured and competitive non-residential education mill rate, can result in cuts to municipal and library mill rates and improved services as the per capita non-residential assessment base in the province grows. Simultaneously, this change could grow provincial government revenue. That is a virtuous cycle.

The City of Red Deer experience also demonstrates this concept. The combined (municipal and education) 1997 mill rate for residential property in Red Deer was 16 mills. In 2009, the rate is 7.41 mills. In 1997, the combined (education and municipal) non-residential mill rate in Red Deer was 21 mills, and in 2009 it is 15.7 mills. No jurisdiction in Saskatchewan has seen this size of property tax rate decline in any of their mill rate levels in any category of property. Even with these mill rate cuts, the overall assessment growth provided more money for education and municipal services. In 2001, Red Deer generated about $52 million in property taxes. In 2008, Red Deer generated $102 million in property taxes.

Three examples of wealth effect are appended to this document in appendix 6.

9. A Start on the Path to a Virtuous Cycle

At the next provincial reassessment, a number of provincial property policy changes will be required to foster the desired virtuous cycle of wealth generation. In the meantime, we propose an interim measure to accelerate investment, improve competitiveness, and do so without requiring additional provincial treasury funds but in, fact, grow additional provincial government revenues.

We propose that, beginning immediately, all new non-residential and/or property construction or expansions of existing investments should be taxed for education purposes at the 2010 residential education mill rate, but on 100 per cent of assessed value. This 9.51 mill rate would be applied only to any incremental property assessment derived from start-up, construction or expansion. Because this new and more competitive mill rate will only apply to incremental taxable assessment, this policy change places no additional burden on the provincial treasury.

Applying this interim rate could allow Saskatchewan to achieve full education taxation competitiveness with Alberta for residential and non-residential property by 2017 without any additional treasury burden. Applying a single mill rate to all non-residential property by at least 2013 is an important policy change because of the investment distorting characteristics of a discriminatory wealth tax like property tax embedded in the interim measure.

This approach also addresses the income tax deductible treatment of property taxes for businesses as compared to residential property and so, albeit in a cumbersome and indirect manner, improves the tax treatment equivalency between residential and non-residential mill rates.

Our Chambers will continue to advocate for improved property policies, taxation transparency and competitiveness in 2013, but in this report our Chambers challenge the provincial government to make an important growth-orientated interim tax structure change that will improve Saskatchewan’s growth prospects and competitiveness and improve at least to some extent the underpinning of the current education property tax structure.

There are five measures that will ultimately make Saskatchewan competitive with Alberta in regards to education property taxes. These measures will move Saskatchewan closer to a principle-based education property tax system in the province:

1. Apply a mill rate of 9.51 to all new or expanded non-residential property investment between now and the next reassessment
2. Cap the amount of revenue received from the non-residential properties at the forecast 2010 revenue of $273.5 million until we meet Alberta non-residential mill rates in competitiveness

3. Apply the 2010 residential mill rate of 9.51 mills (or lower if such a rate will still raise $273.5 million in non-residential education property taxes in 2013) to all non-residential property at a single rate at the next reassessment in 2013
4. Reduce the non-residential mill rate on all new or expanded non-residential property to the residential rate (estimated to be 7.36 mills in this report) to be applied at the 2013 reassessment until the next reassessment (currently expected in 2017). And repeat this approach in 2017 by applying the 2013 residential mill rate to all non-residential assessment in 2017 and apply the 2017 rate (predicted to be lower still) to all new and expected non-residential assessment between 2017 and the next reassessment if the changes are still insufficient to result in an Alberta-competitive non-residential education mill rate
5. Consider applying additional general revenues to reduce the revenue required from non-residential properties in 2011, 2012 and 2013 to accelerate the process of building the assessment base.

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Appendices

Appendix 1

Taxation

No	Municipality	Total Property Tax Assessment Per Capita	Percentage Change in Total Property Tax Assessment Per Capita	Non-residential Property Tax Assessment Per Capita	Percentage Change in Non-residential Property Tax Assessment Per Capita	Residential Tax Burden (per dwelling)	Change in Residential Tax Burden (Per Dwelling)
		Average 2005-2007	Average 2004/05-2006/07	Average 2005-2007	Average 2004/05-2006/07	Average 2005-2007	Average 2004/05-2006/07
1	Halifax Regional Municipality	$64,912	8%	$14,844	1%	$1,319	6%
2	Saint John (NB)	$86,880	-5%	$56,340	5%	$1,439	7%
3	Fredericton	$77,811	5%	$16,810	5%	$1,681	9%
4	St John's	$73,418	8%	$24,748	6%	$1,557	3%
5	Charlottetown	$60,294	8%	$14,366	4%	$1,346	9%
6	Gatineau	$63,569	14%	$13,732	7%	$1,068	
7	Laval	$70,230	16%	$14,274	9%	$1,906	5%
8	Longueuil	$73,901	-5%	$14,370	-7%	$666	
9	Montreal	$79,025	6%	$20,219	1%	$1,783	
10	Quebec	$57,747	11%	$14,159	8%	$1,590	4%
11	Sherbrooke	$48,643	15%	$11,385	13%		
12	Barrie	$81,986	9%	$14,153	8%	$2,057	11%
13	Guelph	$84,140	6%	$12,994	6%	$1,943	8%
14	Hamilton	$72,472	7%	$21,921	5%	$2,118	5%
15	Kingston	$76,082	7%	$11,183	5%	$2,728	7%
16	London	$69,442	7%	$10,657	4%	$1,822	7%
17	Ottawa	$100,728	7%	$23,775	6%	$2,088	5%
18	Greater Sudbury	$50,003	4%	$9,472	2%	$1,693	6%
19	Thunder Bay	$55,260	3%	$10,976	1%	$1,752	4%
20	Toronto	$120,907	5%	$23,599	4%	$1,779	4%
21	Windsor	$68,058	3%	$14,422	3%	$1,639	5%
22	Winnipeg	$46,397	8%	$12,464	5%		
23	Regina	$44,175	6%	$17,537	4%	$1,050	7%
24	Saskatoon	$39,474	6%	$11,842	6%	$776	6%
25	Calgary	$131,024	24%	$28,699	24%	$865	9%
26	Edmonton	$92,010	15%	$20,494	15%	$952	10%
27	Burnaby	$153,758	18%	$29,356	13%	$851	6%
28	Richmond	$164,128	18%	$34,649	14%	$962	6%
29	Surrey	$119,647	20%	$13,748	15%	$777	6%
30	Vancouver	$194,468	19%	$32,428	13%	$890	11%
31	Victoria	$155,748	17%	$37,178	10%	$802	6%
	Minimum	$39,474	-5%	$9,472	-7%	$666	3%
	Maximum	$194,468	24%	$56,340	24%	$2,728	11%
	Average	$86,333	9%	$19,574	7%	$1,445	7%

Non-residential Tax Burden Per Capita	Change in Non-residential Tax Burden Per Capita	Non-Residential Tax Revenues as a proportion of Own Source Revenues	Percentage Change in Non Residential Tax Revenues as a proportion of Own Source Revenues
Average 2005-2007	Average 2004/05-2006/07	Average 2005-2007	Average 2004/05-2006/07
$234	1%	16%	-4%
$496	6%	39%	-2%
$355	6%	25%	-3%
$262	2%	18%	-11%
$345	5%	27%	0%
$290		18%	
$542	2%	37.44%	
$167		7%	
$892		39%	
$581	6%	32%	-1%
$245	7%	14%	4%
$316	9%	16%	2%
$300	2%	15%	-3%
$863	8%	38%	2%
$264	5%	14%	-3%
$376	2%	17%	-2%
$313	7%	17%	0%
$807	1%	28%	-5%
$535	2%	21%	-5%
$660	3%	28%	0%
$937	8%	61%	2%
$153	4%	7%	-7%
$553	12%	28%	1%
$425	8%	23%	0%
$378	8%	26%	-1%
$346	10%	21%	-10%
$115	21%	10%	13%
$566	-7%	32%	-12%
$513	9%	26%	2%
$115	-7%	7%	-12%
$937	21%	61%	13%
$442	6%	24%	-2%

Source: Atlantic Institute of Market Studies[15]

Appendix 2

A CRITIQUE OF
"A DECISION FOR OUR FUTURE"

A report dated January 2009 by the Legislative Secretary to the Minister of Education.

As part of the Greater Saskatoon Chamber of Commerce and Regina and District Chamber of Commerce analysis of the 2009 education property tax policy, this appendix is designed to critique some of the underlying assumptions embedded within the report (*A Decision for Our Future*) upon which the Government of Saskatchewan based its current education property tax rules.

It was the report that resulted in the complex and cumbersome tiered mill rates for commercial properties now in place. To the report's credit, it did cause a significant change to the education property tax rules in Saskatchewan, something that had not been undertaken by successive governments for over 30 years. Over previous decades, the Government of Saskatchewan had received numerous recommendations regarding how to potentially address the shortcomings of Saskatchewan's education property tax rules but all previous work resulted in no changes in the education property tax system.

Although the report brought about significant changes, it is far from perfect. Indeed, a fundamental assumption to the document is flawed and the application of the formula embedded in the report is complex and cumbersome. The report lacks a sound taxation policy base. These shortcomings as embedded in the current education property tax rules resulted in the creation of this joint chamber study because of the absence of a sound taxation policy base, its uncompetitive result, and the cumbersome nature of the current rules.

The first and foremost flaw in the report is an assumption that a given percentage of education funding is correctly derived from property assessment. This analysis is described on page 10 of the report. The underlying assumption to the report attempts to benchmark a "fair share" based on a comparative of percentage of K-12 educational funding derived from British Columbia, Alberta, Manitoba and Ontario can lead to an "appropriate level" of property tax derived education funding. This assumption is fundamentally flawed. The flaw is that the property assessment base of the respective province is materially different from province to province or jurisdiction to jurisdiction. For example, the per capita non-residential assessment base in Calgary is $28,699 and in Edmonton, it is $20,494. In Regina, the non-residential assessment per capita is $17,537 and in Saskatoon, it is $13,255. Alberta has $ 128.9 billion in non-residential assessment while Saskatchewan has $18 billion in non-residential assessment. The report correctly notes that Saskatchewan has been overly dependent on property taxes to fund government services including education. Most particularly, the report notes that this has been particularly true for non-residential investments in Saskatchewan. Over time, and as demonstrated in this joint study, property taxes alter behavior to avoid tax loads and result in smaller assessment base. The significant difference in assessments per capita between jurisdictions with Saskatchewan's assessment per capita being lower than Alberta means that the property tax capacity in Saskatchewan is lower. The relatively higher tax rates in Saskatchewan have predictably and notably depressed property investment and property values over time so that the per capita assessment base in Saskatchewan is much lower than our competitor jurisdiction Alberta.

These effects are also demonstrated in comparison against other Canadian cities with lower property tax rates. The property assessment per capita in Saskatchewan as approximated by the two largest cities is $44,175 in Regina and $39,474 in Saskatoon. This compares to a Canadian average of $86,333. This data was derived from the Atlantic Institute of Market Studies (AIMS) 2009 report comparing thirty-one cities in Canada.

These depressed and diminished Saskatchewan values are also anecdotally verified in farmland market values in Saskatchewan compared to Alberta. The AIMS study shows that tax rates have modified behavior. The attempt to approach Alberta's percentage of education funding derived from property taxation on the smaller Saskatchewan property assessment base just reinforces a vicious cycle of continuously higher effective tax rates in Saskatchewan. This results in comparatively less investment over time and less reinvestment and an even lower assessment base relative to Alberta and in turn resulting in even higher effective rates as Saskatchewan attempts to hold a certain percentage of education funding derived from an even smaller per capita assessment base.

A longer term solution to property and tax policy needs to be designed around creating a "virtuous cycle" wherein low effective rates encourage investment thus growing the assessment per capita and consequently lowering effective property tax rates to generate the same amount of tax revenue while encouraging even more investment in the future. A positive feedback loop of reinvestment and new investment could build an even larger tax assessment base. The underlying and faulty assumption to the report can be simplified and taken to the extreme that: If there was only one assessed property in Saskatchewan, it should pay $525,600,000 per year in taxes (30 per cent of $1,752,000,000) to fund education regardless of that property's assessed value.

In contrast the "Wealth Effect" section of this document identifies the benefits of creating a virtuous cycle of reinvestment and tax base expansion in Saskatchewan.

The remainder of the critique will centre on the tiered mill rate structure and demonstrate how the report itself notes that the applied rules are at odds with the only proxy of property taxation policy in place and as adopted by the Ministry of Municipal Affairs. The current approach also contradicts other stated goals of the Government of Saskatchewan concerning an aversion to capital taxes and an interest in promoting Saskatchewan competitiveness through growth oriented taxation policy. The tiered mill rates now in force have no basis in horizontal or vertical equity as concepts in tax policy; neither can a benefits received agreement be used to support the current system. The current rules are overly complex, again in conflict with good tax policy. The report does not address any competitiveness issues in the context of how a business attracts capital and competes with competitors in other jurisdictions, most noticeably, those competitors in Alberta, even though that was the stated objective of the report.

This critique challenges the observation contained within the Report that the 2009 applied education property tax rules meet the government's commitment on this issue. In fact, the current rules do not meet the provincial government's tax relief commitments or the commitment to reduce the adverse capital tax impact on investment attraction. The current government has consistently indicated that it is sensitive to the impact of all capital taxes in general and property taxes specifically (as capital taxes - a wealth tax has been demonstrated to be the most harmful form of taxation toward investment attraction). Despite the stated concern by the Government regarding capital taxes, the component of the economy that attracts property tax and is most sensitive to a capital tax's adverse effects is non-residential (commercial/industrial) property. This is the very (non-residential) category of property that remains most adversely affected under the current formula.

The letter of transmittal of this report to the Minister by Legislative Secretary to Minister indicates that a provincial infrastructure tax or provincial property tax might more accurately reflect the property taxation system proposed within the report. Whether current taxation formula is labeled education property tax or an infrastructure tax is irrelevant. This formula is flawed in its lack of a sound policy base and harmful in its adverse impact on investment attraction.

The report indicates that taxation fairness is essential. On page 3, the report states, "Tax effort should be similar, regardless of where a property lives, farms or operates a business." This statement falls short on fully articulating the concept of taxation equity from a vertical and horizontal perspective, but even under the report's simplistic description of equity, the recommended approach is flawed. The report then goes on to indicate that the previous system (prior to 2009) was overly dependent on property taxes to fund education and that this burden fell disproportionately on non-residential property. On page 5 of the report, "In comparison to other provinces and relative to other property tax classes, Saskatchewan is somewhat over reliant on commercial industrial assessment to fund K-12 education and the total tax burden is greater." Yet in the final recommendation, non-residential property is the property category least addressed by the Report in terms of tax burden relief.

On page 11, the report notes that commercial and industrial properties are taxed at 100% of assessed value. Residential properties are taxed at 70 per cent of assessed value cultivated agricultural land is taxed at 55 per cent and pastureland is taxed at 40 per cent. The report notes that these percentages of value remain the only approximate statement of provincial property tax policy. Given that this is the only evidence of property tax policy for the current government, the mill rates that are applied in the final report are in direct conflict with the only proxy of property tax policy descriptive in existence in Saskatchewan.

While the progress made concerning education property tax in Saskatchewan is significant compared to 30 years of inaction, the current approach is inconsistent with the provincial government's objectives and fails to meet accepted taxation policy principles. The current rules contradict stated objectives of the government regarding concerns over capital tax and competitiveness. The current approach also more than disproportionately and adversely offsets the only explicit property tax policy in place. For these reasons, the current education property tax application will need to be amended in the near future particularly with regard to new or incremental property investment in Saskatchewan.

The government's percentages of value property taxation approach now in place can serve as a foothold from which the province can correct the flaws in the current approach as it applies to new or incremental non-residential assessment as a growth including tax structure.

Appendix 3

Arguments against wealth tax

A 2006 article in *The Washington Post* titled "Old Money, New Money Flee France and Its Wealth Tax" pointed out some of the harm caused by France's wealth tax. The article gave examples of how the tax caused capital flight, brain drain, loss of jobs and, ultimately, a net loss in tax revenue. Among other things, the article stated, "Eric Pichet, author of a French tax guide, estimates the wealth tax earns the government about $2.6 billion a year but has cost the country more than $125 billion in capital flight since 1998." And wealth taxes generally have high management costs, for both the taxpayer and the administrating authorities, compared to other taxes. According to one study in the Netherlands the aggregated cost of the tax's yield was roughly five times that of income tax.

Source: Wikipedia[14]

Appendix 4

A Scenario for Growth - Building a Business Climate for Growth Through More Competitive Business Education Property Taxes

This appendix details a scenario under which the interim solution proposed in this report could be applied over the next decade to achieve education property tax load competitiveness for residential and non-residential property in Saskatchewan. Under the scenario, this objective can be achieved without reducing the contribution from education property tax from any of the property categories.

The scenario begins with the education property tax contribution from each of the categories remaining fixed at 2010 levels:

	2010 Contribution	Mill Rate
Agriculture	$38,600,000	3.91
Residential	$257,700,000	9.51
Non-Residential	$273,500,000	15.10*

*Weighted Average Mill Rate

The nominal non-resident assessment for Saskatchewan is approximately $18 billion.

($273.5 million ÷ 15.10 mills)

The nominal residential assessment for Saskatchewan in 2009 is approximately $38.7 billion.

($273.1 million ÷ 10.08 mills) ÷ 70% taxable assessment)

As noted earlier in the report, the nominal assessment is based on June 2006 valuation and can be adjusted by 30 per cent to establish an estimate of 2009 effective current market assessment for both residential and non-residential assessment.

This adjustment results in an estimated 2009 value for residential assessment of $50 billion and an estimated 2009 value of non-residential property of 23.5 billion.

Even if there is no growth in the value of assessment of either of these property categories at the next assessment in 2013 from the 2009 valuation, the following analysis applies in order to generate the 2010 levels of property tax revenues from each of these categories. Based on the 2009 estimate, effective residential assessment will result in a mill rate of 7.36 mills for residential property [$257,700,000 ÷ ($50,000,000,000 x .7)] in 2013. And 11.64 mills for non-residential property. [273,500,000 ÷ 23,500,000,000]

Our chambers contend in 2013 that the proposed interim solution will stimulate non-residential investment in the province over the next four years. Projects under consideration in Saskatchewan in various industries about which our chambers are familiar support this contention. The Alberta non-residential investment comparative also suggests that such growth potential is achievable in a real market situation thus removing this scenario from purely an abstract concept.

In order for all non-residential properties to generate the 2010 level of education property tax revenue in 2013 but applying the 2010 residential mill rate of 9.51 mills to all non-residential investment in Saskatchewan will require that non-residential assessment will have to grow by $5.3 billion. This would grow the effective non-residential assessment of $23.4 billion ($18 billion in 2006 nominal non-residential assessment adjusted to 2009 values by increasing the value by 30 per cent) to a total of $28.7 billion by 2013.
($273.5 million ÷ 9.51 mills)

This, in our Chambers' view, is quite achievable with the implementation of the recommended stimulative mill rate of 9.51 for non-residential new or expanded real property investment in the province between 2009 and the reassessment in 2013.

If the 2013 theoretic residential mill rate of 7.36 mills is again applied to all new or expanded non-residential real property investment between 2013 and 2017 and holding education property tax revenue funding is constant, the investment growth in non-residential assessment required to achieve the 7.36 mill rate (projected 2013 residential mill rate) to be applied to all non-residential assessment in 2017 (assuming the four year assessment cycle remains) is projected to be $8.46 billion in new investment between 2013 to 2017. This results in a projected non-residential assessment of $37.16 billion for the level to be sufficient to raise $273.5 million in 2017 at the residential mill rate of 7.36 mills (the projected 2013 residential mill rate). ($273.5 million ÷ 7.36 mills)

This objective also is believed to be achievable by 2017 based on projects now under consideration in Saskatchewan and based on the Alberta comparative test for reasonability.

Stretching past 2017 projections for this analysis becomes difficult to apply with any certainty. However, if a similar analysis is applied within the interim mill rate capped at the residential mill rate in 2017 for all incremental non-residential real property investment between 2017 and 2021 it suggests that both residential and non-residential mill rates can approach the Alberta 2009 rates of 3.39 mills for residential and 4.98 mills for non-residential property by 2021. These mill rates could still provide education property tax derived funding levels from education property tax revenues with the education property funding at the 2010 funding levels that the Government of Saskatchewan presented in its March 2009 budget.

Our Chambers will continue to advocate for further general revenue funding contribution to allow for further education property tax relief could accelerate this investment growth cycle and thus accelerate significant societal benefits of accelerated business investment.

The sooner that education property tax levels become competitive for business investment, the faster the province will grow opportunities for our citizens. And we believe this can occur without harming farmers or the education system. Indeed the wealth effect section of this report shows how all citizens of this province can benefit from a competitive and principle based education property tax system**.**

Appendix 5

Illustration of METR calculation, September 28, 2009

2008 METR	**SK**	**AB**
	28.60	22.00

Assumptions:

Marginal investment of $500,000
Combined corporate tax rate of 31.5% (SK); 29.5% (AB)
Effective Education Property tax = 1.12% (SK); .50% (AB)
Required after tax rate of return 12% or $60,000
X = before tax rate of return or before tax income (BTRR)

Step 1 – illustrate how METR is used to determine BTRR
(X-.12)/x = METR (divide each side by x)
X-.12=.29X (transpose)
.71X = .12
X=16.9%

Now, using $60,000 required income
X= 60,000+.29X
.71X = 60,000
X = 84,500
84,500/500,000 = BTRR of 16.9%

Step 2: Introduce an education component of a property tax subject to a deduction for income tax purposes

Education Property Tax = $5,600
Income tax rate = 31.5%

X = 60,000 + (100-31.5)*5,600 + .29 X

.71X=63,836
X= 89,910

89910/60000 = 18% = Before Tax Rate of Return

Step3: calculate METR

(BTRR-AFTR)/AFTR=METR
(.18-.12)/.18 = 33.3% Saskatchewan

Repeat for AB – change effective property tax rate and corporate income tax rate

Appendix 6

Examples of the Wealth Effect

Three excerpts from the Greater Saskatoon Chamber of Commerce June 2003 study on education property taxes provide further evidence of this wealth effect. The first example demonstrates tax avoidance behaviour. The second demonstrates a desired response to a tax policy change (even if the unintended result of assessment policy flaws, as was in this example). Example three provides a specific case to illustrate the wealth effect on an individual property.

<u>Example 1:</u> (Page 14)
"In a one year period, from May 1997 to May 1998, $2.3 billion was invested in agribusiness value-added processing in the prairie provinces by business. Less than 18% of this investment was attracted to Saskatchewan, even though the farm land base of Saskatchewan is far larger than either Alberta or Manitoba and land costs were lower. Because of the highly capital intensive nature of agri-value added building investments, the findings of this study clearly suggest that Saskatchewan's lack of success in attracting agri-value investment is, to a substantial extent, related to the current provincial property tax policies, and the aversion of these kinds of investment to higher property taxation jurisdictions."[15] This observation is further buttressed by the 2008 KPMG Competitive Alternative Study, which notes that while the overall cost index in Saskatchewan is highly competitive, the exceptions are property taxation levels and sales tax treatment.

<u>Example 2:</u> (Page 23)

"(As a result of the 1997 reassessment), hotels in Saskatchewan in 1997 were assessed on an "artificially low basis" (although competitive with Red Deer's 1997 effective tax rate of 2.1 per cent), although this "low" tax rate was the result of flaws in the assessment system (see 2.2.1a). A competitive effective property tax rate for this industry caused a dramatic expansion and investment in the hotel industry across the province and in Saskatoon in particular (from 1997 to 2001). These "low valuations" in the industry attracted investment. In Saskatoon this was well illustrated where there was a 25 per cent increase in hotel room inventory in the four year period. This gain in investment in Saskatoon was partially the result of the lowered property tax rate. After the 1997 assessment, there was also a surge of hotel improvements throughout Saskatoon. This incremental investment, in turn, expanded the property assessment base of Saskatoon. The implications of current tax loads on hotels and the hotel industry aside, this example illustrates the wealth effect. The hotel assessment base in Saskatoon was substantially increased as a result of the effective tax cut for hotels in the 1997 reassessment. In 1997, the hotel/motel assessment base equaled $46,000,000 in Saskatoon. In 2001, the assessment for hotels and motels measured $136,000,000 in Saskatoon. As a result, this assessment category grew faster than any other category of property with a growth of 295 per cent in just four years. This growth rate in assessment was substantially faster than any other business types (which didn't have the benefit of the artificially low hotel property assessment levels).

<u>Example 3:</u> (Page 24)

"Another example of the wealth effect deals with a Saskatoon commercial property that was assessed prior to 1997 such that the tax load (prior to the 1997 assessment) was $52,000 per year, but (the property) sold for $50,000 at auction (in 1996). In 1997, the property value would be assessed under the new assessment, if accurate, at $50,000, which would then be paying approximately $2500 (with a 5 per cent effective tax rate) in property taxes. As a result of the adjustment, the owner determined that it made sense to invest approximately $650,000 in the property to turn it into a multi-unit rental residential property with commercial property on the main floor. There was a drastic increase in investment in the property which now generates approximately $35,000 in new annual property tax revenue in Saskatoon. The tax source cost of reassessment in 1997 for this property was large, but was almost completely offset by the new investment as a result of the wealth effect. In this real world example, Saskatoon's employment base was stimulated by the new investment and the rental housing unit supply for Saskatoon was increased and there was a rebound in the tax revenues on the property. This is the wealth creation effect in action."[15]

Appendix 7

The following analysis is available from the Competitive Alternatives website (www.competitivealternatives.com) and illustrates the costs of various factors in location analysis.

11/23/2009 Competitive Alternatives - Detailed Res...

COMPETITIVE ALTERNATIVES.COM COST MODEL
DETAILED COMPARISON REPORT

INDUSTRY: OVERALL RESULT **RUN DATE: 23/11/2009 10:30:44 AM**

OPERATION: Average of 12 operations
(USD$'000)

City	Moose Ja	Prince A	Red Deer	Regina	Saskatoo
Region	SK	SK	AB	SK	SK
Country	CA	CA	CA	CA	CA
Exchange rate per USD$	C$1.000	C$1.000	C$1.000	C$1.000	C$1.000
Initial Investment					
Land	94	383	1,063	799	1,095
Buildings	3,185	3,098	3,683	3,185	3,402
	3,279	3,482	4,746	3,984	4,497
Rank, total investment	*1*	*2*	*5*	*3*	*4*
Cash	238	238	238	238	238
Inventory	1,125	1,125	1,125	1,125	1,125
Fixed assets	4,710	4,710	4,710	4,710	4,710
	$9,353	$9,555	$10,820	$10,058	$10,570
Initial Financing					
Debt	4,658	4,770	5,462	5,045	5,326
Equity	4,694	4,786	5,358	5,013	5,244
	$9,353	$9,555	$10,820	$10,058	$10,570

10-Year Average Profit & Loss

	Moose Ja	Prince A	Red Deer	Regina	Saskatoo
Sales	17,762	17,852	17,990	18,102	17,981
Location-sensitive costs					
Salary and wages	5,226	5,153	5,533	5,611	5,549
Statutory plans	315	313	333	326	324
Other benefits	1,061	1,046	1,140	1,139	1,126
Total labor	6,602	6,512	7,006	7,075	6,999
Rank, total labor	*2*	*1*	*4*	*5*	*3*

competitivealternatives.com/.../reports.... 1/3

Facility lease	115	263	295	394	263
Rank, facility lease	*1*	*2*	*4*	*5*	*2*
Road freight	636	688	577	644	639
Air freight	23	22	20	22	21
Sea freight	93	97	91	94	96
Total transportation	751	807	687	760	757
Rank, transportation	*2*	*5*	*1*	*4*	*3*
Electricity	183	183	304	183	183
Gas	92	92	81	92	92
Telecommunications	31	31	31	31	31
Total utilities	306	306	415	305	305
Rank, electricity	*1*	*1*	*5*	*1*	*1*
Rank, gas	*2*	*2*	*1*	*2*	*2*
Rank, telecommunications	*4*	*4*	*3*	*1*	*1*
Total operating costs	7,774	7,887	8,404	8,534	8,324
Rank, operating costs	*1*	*2*	*4*	*5*	*3*

	Moose Ja	Prince A	Red Deer	Regina	Saskatoo
Interest	-183	-169	-69	-96	-91
Depreciation	803	797	836	803	818
Total interest, depreciation	620	628	768	707	727
Income tax, national	460	450	367	369	388
Income tax, regional	257	252	299	196	208
Income tax, local	-	-	-	-	-
Capital tax, national	-	-	-	-	-
Capital tax, regional	-	-	-	-	-
Sales tax	95	95	-	95	95
Property tax	112	131	85	132	99
Gross receipts tax	-	-	-	-	-
Business tax	-	-	-	-	-
Grants, subsidies	-	-	-	-	-
Total taxes (net of grants)	924	927	751	791	790
Total location-sensitive costs	9,317	9,443	9,922	10,032	9,840
Location-insensitive costs					
Materials	4,661	4,661	4,661	4,661	4,661
Other operating expenses	1,240	1,240	1,240	1,240	1,240
Total location-insensitive costs	5,902	5,902	5,902	5,902	5,902

Total costs	15,219	15,345	15,824	15,934	15,742
Net profit after tax	$2,543	$2,507	$2,166	$2,169	$2,239
% of sales	14.3%	14.0%	12.0%	12.0%	12.5%
Overall rank	***1***	***2***	***4***	***5***	***3***
Overall index	***93.5***	***94.2***	***97.2***	***97.8***	***96.7***

Summary Measures

	Moose Ja	Prince A	Red Deer	Regina	Saskatoo
Net profit before income tax	3,261	3,210	2,833	2,733	2,836
Effective income tax rate	22.0%	21.9%	23.5%	20.7%	21.0%
Rank	*4*	*3*	*5*	*1*	*2*
Property-based taxes per sq.ft.	$1.51	$1.77	$1.14	$1.79	$1.34
Rank	*3*	*4*	*1*	*5*	*2*

Effective tax rates are not shown where results are not meaningful due to marginal profitability.
Effective tax rates may be negative due to refundable tax credits exceeding taxes paid.

Operating Specifications

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The analysis on this website is based on cost information collected primarily between July 2007 and January 2008. Taxes reflect tax rates in effect on January 1, 2008, and also incorporate any announced changes at that time to take effect at specified later dates. Exchange rates and other cost factors will, of course, change over time. Tax rates and other tax-related information are also subject to change as a result of new legislation, judicial decisions, and administrative pronouncements.

All information provided is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act upon such information without appropriate professional advice after a thorough examination of the particular situation.

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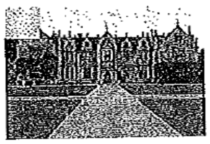
Appendix 8

Investment Decision: Expand (Double) in Saskatoon or Build New in Red Deer?

Industry	Investment Amount	Saskatoon		Red Deer		Difference		Decision
		Nominal	Effective	Nominal	Effective	Nominal	Effective	
Overall Industry Average	$4,497,000	$79,211	$54,319	$22,395	$22,395	$56,816	$31,924	**Red Deer**
Manufacturing Average	7,708,000	142,984	105,100	38,386	38,386	104,598	66,714	**Red Deer**
Aerospace	8,013,000	148,641	109,924	39,905	39,905	108,736	70,019	**Red Deer**
Agri-Food	5,304,000	96,440	95,937	26,414	26,414	70,026	69,523	**Red Deer**
Automotive	10,258,000	190,286	140,952	51,085	51,085	139,201	89,867	**Red Deer**
Chemicals	5,304,000	96,440	67,082	26,414	26,414	70,026	40,668	**Red Deer**
Electronics	12,941,000	230,894	168,658	64,446	64,446	166,448	104,212	**Red Deer**
Metal Components	9,846,000	182,644	135,292	49,033	49,033	133,611	86,259	**Red Deer**
Pharmaceuticals	7,025,000	130,314	94,299	34,985	34,985	95,329	59,314	**Red Deer**
Precision Manufacturing	3,182,000	51,135	37,124	15,846	15,846	35,289	21,278	**Red Deer**
Telecommunications	6,365,000	118,071	83,862	31,698	31,698	86,373	52,164	**Red Deer**
Plastics	10,358,000	192,141	142,326	51,583	51,583	140,558	90,743	**Red Deer**

Appendix 9

The following excerpt illustrates that real estate investment behaviour is heavily influenced by taxation and that this behavioural influence has existed for centuries.



England's Window Tax

January 16, 2007 by **Renaissance Woman**

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An Unusual Tax with Some Unusual Consequences

In the 1690's, British lawmakers were posed with an interesting problem: how to tax their citizens on their income, without knowing too exactly just what that income was.

The emotional climate at the time was vigorously opposed to an income tax. The objection to an income tax wasn't based so much on an objection to paying, but to having the government know how much income one had in the first place. It was considered intrusive, an invasion of privacy, and an attack against personal liberty.

Still, it stood to reason that some kind of taxation had to be made based in some way on the relative prosperity of the taxpayer. What to do, what to do..... Finally some genius came up with a brilliant solution: We'll count their windows!

This wasn't as bad an idea as it might sound. First of all, the number of windows in a dwelling did bear some relationship to the size of the structure. And the size of the home was related to the wealth of the homeowner. Also, glass was expensive, and it stood to reason that one didn't put a lot of windows in one's home unless one could afford it. And you have it admit, it was pretty easy to assess taxes!

This tax led to some of the unusual features of English architecture in this period. Have you ever seen pictures of English houses or pubs where some of the windows have been bricked up? If the structure is old enough, that well may have been the work of an early tax avoider. Some of the new buildings that were erected in the late 17th and early 18th century were built with a minimum of windows; in fact, some bedrooms had no windows at all!

On the other hand, the truly rich who wished to flaunt their wealth had a tendency to build home with as many windows as possible. In some cases, they even included non-functional windows, erected on top of a structural wall.

The window tax continued in England until 1851, when it was repealed in favor of a more ordinary tax based on overall property values. Some believe that the phrase "daylight robbery" may have its origins in the creation of the window tax, although others argue that the phrase did not come into popular usage until much later.

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