The Impact of HST on Rental Housing in Ontario

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frpo

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INTRODUCTION

Mike Chopowick: Good afternoon, my name is Mike Chopowick, Manager of Policy for FRPO. FRPO is the Federation of Rental-housing Providers of Ontario, and we represent landlords and property managers who provide over 250,000 rental housing suites across the province. Our President, Vince Brescia, sends his regrets as this afternoon FRPO is hosting its annual awards Gala, where we recognize excellence and professionalism in the provision of rental housing.

EXECUTIVE SUMMARY

FRPO appreciates the opportunity to provide input on the *Ontario Tax Plan for More Jobs and Growth Act, 2009* that will directly affect landlords and tenants in Ontario.

Today I will be explaining to you why the implementation of the HST, as currently being planned, will be devastating for the rental housing industry, and for the rental experience of our customers.

We appreciate the position put forth by numerous business groups and economists that harmonizing the provincial PST with the GST is a way to make Ontario a more internationally attractive place to invest and provide long-term economic benefits to our province. We also recognize the corporate tax reductions in the provincial budget, and commend the government for this positive initiative.

In the course of implementing a more competitive tax system, however, the provincial government overlooked the acute negative impact on the rental housing sector.

Let me start by explaining why the HST impacts our sector so negatively. I will conclude by recommending options for mitigating this impact.

HST IMPACT

Residential rental housing is one of the few types of businesses in Canada that is 'GST-exempt'. This means landlords pay GST on their inputs, but do not collect GST on rents. In addition, there are no input tax credits for rental housing. Rents were not treated like groceries, which are "zero-rated". For groceries, sellers are given input tax credits so that there is no sales tax passed on to the customer.

When the HST is implemented, it will increase our industry's operating costs by about 4.8 percent. This means that a new eight percent in new taxes will be applied to about 60 percent of our costs. Expenditures on heat and hydro, maintenance contracts, property management fees, legal, accounting, elevator repairs, snow removal and landscaping are all examples of rental housing costs that will subject to an 8 percent increase in taxes.

When you add in a forecast for regular inflation in that year by TD Economics, we expect our costs to rise by 6.5 percent, or about $400 for every rental unit in the province. That is a huge impact, with serious consequences.

On top of this, rental housing is rent controlled in Ontario. That means that landlords will not be able to pass on this huge cost increase. They will be hit with a $400 cost increase that they cannot recover.

Let me explain why $400 per home is a huge negative impact, and why the province should care about this impact.

REDUCED REPAIRS AND MAINTENANCE

If you look at the budget of a rental building, you quickly realize that most of the expenditure lines are not discretionary. Property taxes, mortgage payments, heat, hydro, insurance. Even staffing levels are not discretionary, as it is a capital intensive business, not labour intensive. At the end of the day, there is only line item that is discretionary: repairs and maintenance. A $400 reduction in repairs and maintenance represents a 45 percent reduction in the repairs and maintenance budget for a typical rental building.

As it is currently being planned, the HST will result in a massive deferral of repairs and maintenance of the rental stock across Ontario. This is a horrible outcome when you consider that we have an ageing rental stock in Ontario. Engineering studies have shown that the rental stock in this province has huge deferred maintenance issues, and large investments in the stock are required to ensure its future viability.

You may not be aware of this, but the industry's net operating income (NOI) has been declining for the past 10 years. Over the last ten years, the NOI of a typical rental building in Ontario has declined by about 16%. The HST impact will be on top of this.

Some in the government point to corporate tax reductions as an offset. However, a huge portion of the rental housing industry is made up of sole proprietorships, limited partnerships, income trusts and pension funds, none of whom get an offset through the proposed corporate tax changes.

This has several negative implications for tenants in Ontario:

- They will see a decline in the thing that they care about most in their units – repairs and maintenance;
- Customer service standards will decline;
- The condition of their buildings will deteriorate;
- Future investment in rental housing will decline; and
- Finally, all these costs will ultimately be passed on to tenants, even though not all in the short term. This will be done immediately on

non-controlled units, on turnover, and through above guideline increases.

The bottom line is that the HST will have a huge negative impact on the residential rental sector, reducing jobs, investment and repairs and maintenance.

SOLUTIONS TO THE HST IMPACT

Zero-Rating. The preferred solution for the rental housing industry is a zero-rating. This is a consistent position put forward federally by the Canadian Federation of Apartment Associations, so it is not a new proposal for our industry. There is a strong argument for fully removing rental housing from the tax base for the proposed HST.

The justification for rental housing to receive the same type of treatment as basic groceries would be similar to the justification for zero-rating groceries: shelter (especially rental housing which is predominantly occupied by low and middle-income people) and food are basic necessities and a tax on such goods and services is regressive.

We recognize the measurable cost this would have to both the federal and provincial governments in terms of tax revenue.

Industry Assistance Program. A second solution is to compensate the industry for the negative impact, which could be done through input tax credits or any other form of financial assistance. We recognize this requires funding. However, the industry needs at least some transitional assistance to mitigate this sudden negative impact.

Reform Rent Control. The third solution would require the government to fix the rent control guideline to allow the industry to pass on the HST cost. The main rationale for doing this is not just related to the HST, however. Fixing Ontario's rent control system is necessary to simply allow landlords to recover all normal operating cost increases we face. Ontario's rental housing stock is aging, and requires more investment to be maintained, not less. But, Ontario's current CPI rent guideline doesn't even allow for recovery of normal industry costs. As evidence, we are projecting the 2011 rent guideline to be at or near 0%, while we already know our industry costs will be increasing far above that, likely between 5% and 10%.

In closing, I want to state that any solution will require the government of the day to start caring more about the negative impact of policy changes on landlords. The case of the HST is a clear example of where the fortunes of tenants and landlords are inescapably linked. Regardless of the sales tax exemption of rent, tax rebates paid to tenants and the misguided notions behind rent control, tenants will see and experience a negative impact on their housing from the HST. We recommend that mitigation be provided before this tax is implemented next year, to ensure the ongoing affordability and quality of Ontario's rental housing stock.

Thank you for the opportunity to speak to this matter today.