



TORONTO STAFF REPORT

March 31, 2004

To: Administration Committee
From: Chief Financial Officer and Treasurer
Subject: Overpayment of Property Taxes

Purpose:

This report provides information and statistical data regarding the tax refund process administered by staff of the Finance Department and recommends new operational and process improvements to the tax refund process.

Financial Implications and Impact Statement:

There are no financial implications associated with the recommendations contained in this report.

Recommendations:

It is recommended that:

- (1) all credit balances on property tax accounts resulting from assessment appeals shall be credited or refunded directly to whomever the Tribunal directs in its decision, and if no payee is named in the decision, to the current assessed owner, in accordance with section 341 of the *Municipal Act, 2001*; and where there has been a change in the assessed owner(s) since the date the decision was released by the Tribunal, the Director, Revenue Services, will require an executed Indemnification Agreement in a form satisfactory to the City Solicitor before any refund shall be made;
- (2) credit balances on all tax accounts of less than one hundred dollars (\$100) shall be applied as a credit to the tax account of the current assessed owner of said property, and, where requested in writing, credit amounts between fifteen dollars (\$15) and one hundred dollars (\$100) will be refunded directly to the current assessed owner by way of a cheque;

- (3) for residential tax accounts with credit balances between one hundred dollars (\$100) and one thousand dollars (\$1,000) inclusive, credit amounts shall be credited or refunded to the current assessed owner of the property, upon receipt by the City of a written refund request signed by the current assessed owner, together with an Indemnification Agreement in a form satisfactory to the City Solicitor;
- (4) for all other tax accounts, credit amounts shall be credited or refunded to the individual who made the overpayment, provided the City is in receipt of a written refund request signed by the claimant, together with an Indemnification Agreement in a form satisfactory to the City Solicitor, and proof in a form satisfactory to the Director, Revenue Services or a designate, that the said owner made the payment for which the refund is requested;
- (5) in the event that the City has not received a request for a refund, or a signed Indemnification Agreement and/or proof that the said owner made the payment for which the refund is requested, and no refund is issued by the City, all credit balances shall be transferred to the City's Tax Repayment Account, (re: Account No. 215161); and,
- (6) the appropriate City staff be authorized and directed to take the necessary action to give effect thereto.

Background:

At its meeting held on July 2, 2003, the Administration Committee had before it a communication dated June 16, 2003, from Councillor Howard Moscoe to the Chief Financial Officer and Treasurer (CFO) regarding the overpayment of property taxes, and the process used by City staff to track overpayments and repay those individuals who have overpaid their property taxes. A copy of the above-cited communication is attached as Appendix "A".

The Committee referred the aforementioned communication to the Chief Financial Officer and Treasurer and requested a report to address how many people have overpaid their taxes; when adjustments are made and staff justification therefor; and any statistical information pertaining thereto.

Comments:

The City of Toronto's Finance Department administers over 600,000 property tax accounts and collects approximately \$5 billion in annual property taxation revenue for both municipal and school purposes. In accordance with provincial legislation, property taxes are levied against a parcel of land or property; they are not levied against an "individual". Any outstanding taxes levied against a particular parcel of land form a lien on the property and stay with the property even when the property is sold or changes ownership.

Property tax accounts are established for each parcel of land within the municipality (identified by an assessment roll number), as determined by the Municipal Property Assessment

Corporation (MPAC). A number of transactions occurring throughout a given year may affect the City's property tax accounts, such as billings, payments, appeals, billing adjustments, etc.

On an annual basis the Finance Department:

- issues approximately 1.3 million tax bills;
- processes in excess of 3.6 million payment transactions annually: 1.213 million pre-authorized tax bank payments (PTP), 1.028 million cheque payments, 655,000 bank payments, 405,000 telephone bank payments, 192,000 mortgage payments, and 115,000 customer service counter payments;
- processes approximately 40,000 assessment and tax appeals, and other related billing and phase-in adjustments, resulting in tax reductions in excess of \$200 million; and,
- processes approximately 5,000 tax rebates, representing approximately \$15.8 million, resulting from the various tax rebate programs (Ethno-cultural, Charity, Veterans and Vacancies).

An overpayment of property taxes or a credit balance on a property tax account may arise from various circumstances, with the most common occurrences identified below:

(a) Assessment and Tax Appeals

A successful tax and/or assessment appeal results in the recalculation of the property's tax liability. Pursuant to subsection 37(6) of the *Assessment Act*, and subsection 341(2) of the *Municipal Act, 2001*, the City has an obligation to refund any overpayment resulting from the final disposition of a successful property assessment appeal. Assessment appeals and decisions from the Superior Court of Justice, therefore, will result in adjustments to assessment and a recalculation of the taxes payable.

Section 357 of the *Municipal Act, 2001*, provides that municipalities may cancel, reduce or refund all or part of the taxes levied on land due to building demolition, reclassification, fire etc. Additionally, Section 358 of the *Municipal Act, 2001*, provides that a municipality may cancel, reduce or refund all or part of taxes levied on the land, in one or both of the two years preceding, when a clerical or factual error occurred in the preparation of the assessment roll. In both circumstances, a successful appeal will result in an adjustment to the taxes payable.

(b) Rebate, Deferral and Cancellation Programs

If a property owner applies and is eligible for one of the City's tax relief programs (e.g. vacancy rebate, low-income seniors and low-income disabled tax deferral or tax cancellation programs), the appropriate benefit/rebate amount is applied to the property's tax account based on the established program criteria. The level of tax relief is established by provincial legislation and/or city by-laws.

(c) Multiple Individuals Remit Payment

Circumstances arise where more than one individual pays the taxes on a property, thus creating a credit balance or overpayment on the account. For example, both a mortgage company and the property owner may remit taxes; both spouses remit concurrent payments; upon the sale of a property, a customer on a pre-authorized payment program fails (on a timely basis) to de-enroll from the program, and payment is remitted by both the previous and current owners.

(d) Misapplication of a Payment

- i) When remitting payments, a taxpayer may identify an incorrect assessment roll number resulting in their payment being applied to someone else's property account.
- ii) In addition, Finance staff may misapply a payment to an incorrect assessment roll number. Generally, this type of error is the result of taxpayer remitting a cheque or cash payment without a payment stub or through inadvertent transposition of figures and/or other typographical errors.
- iii) Incorrect site addresses, assessment roll numbers and/or wrong legal descriptions assigned by the Municipal Property Assessment Corporation (MPAC) to property owners on new developments may cause misapplied payments. Also, there have been documented situations whereby an apportionment (where a single property is divided into two or more properties), results in incorrect payments being applied to the former or new tax account(s).

(e) Overpayment of Taxes

Property owner(s) submit payment amount(s) in excess of the property tax liability (as billed), for their respective tax account.

Current Process/Procedures for Tax Refunds:

The Department's current tax refund processes and procedures, outlined below, are consistent with the refund policies and procedures undertaken by the former municipalities prior to amalgamation. These procedures were in accordance with the old *Municipal Act*, R.S.O. 1990, and advice from Legal Services that provided that for the City to best fulfill its statutory obligation to refund overpaid taxes, it should endeavour to return such overpayments to the person who made the payment. Therefore, in order to ensure that the City is refunding the person who paid the taxes, proof of payment and/or a statement of adjustment(s) has always been required.

When a credit balance exists on a property tax account, the City's Finance Department is responsible for reviewing the account and ensuring that any resulting refunds are correctly issued in accordance with any relevant legislation. Given that property tax accounts are linked to parcels of land, rather than individuals, the tax refund process is more complicated and involved

in comparison to the example cited in the attached communication, Appendix “A”, wherein a person’s monthly credit card statement will show any overpayment made on an individual’s account, and then deduct the overpayment amount from the next statement amount due.

As outlined above, there are numerous and complex reasons associated with an overpayment or credit balance to a tax account. Without undertaking a complete review and analysis of the tax account, Finance staff cannot readily identify what caused the creation of a credit balance. Only once staff have determined how the credit balance was created, can the requisite actions be undertaken to address and resolve the overpayment on the tax account.

On a bi-monthly basis, Finance staff generate a credit listing, which identifies tax accounts containing credit balances. Staff perform a review of this listing and conduct an analysis of each identified tax account. Once it has been determined how the credit balance was created, staff first undertake an internal search for the required proof of payment (i.e., where accounts have been paid by a cheque mailed to the City, a scanned image of the cheque can be retrieved). If this documentation cannot be located, a letter is issued to the property owner and/or assigned agent identifying the presence of a credit, the associated tax year, and requesting proof of payment and or a statement of adjustment(s) to substantiate the overpayment. The issuance and tracking of this documentation must be closely monitored to ensure that returned information can be processed in a timely fashion. When the requested proof of payment has been provided by the taxpayer and verified by Finance staff, the overpayment is refunded or credited to the tax account based on the taxpayer’s preference. This refund process can become lengthy, as Finance staff are dependent upon the timely and correct submission of proof of payment information by the taxpayer. If further clarification and/or additional information is required, and/or incorrect or incomplete documentation has been provided, refunds cannot be processed and turn-around times increase substantially. If the requested information has been provided, Finance staff can complete the refund adjustment process within 30 days of receiving information.

It should be noted that proof of payment is not required when a Notice of Decision for an assessment appeal has been received, and a change in the ownership has not impacted the identified parcel of land. Finance staff refund these credits within 30 days of receipt of the Notice of Decision.

The City’s acceptable proof of payment criteria is as follows:

- the front and back of the individuals’ cheque that has been stamped/received by a financial institution,
- statement of accounts and/or supporting financial institution documentation (staff request taxpayers to black-out all other transactions, wherein the City of Toronto is not identified as the payee), or,
- on-line transaction records which identify the City of Toronto as the payee.

All proof of payment information is reviewed by Finance staff prior to the issuance of the overpayment amount, to verify the accuracy of the transaction date, name and amount.

Please reference Appendix “B” - *Refund/Credit Balance Operational Flow Chart*, attached, which provides a visual overview of the current refund process.

Statistical Information:

On an annual basis, the Finance Department processes on average between 30,000 and 52,000 refund type transactions, worth between \$165 million to \$189 million. Table 1, below, identifies and analyzes the number of property tax accounts and the associated dollar amounts relative to residential and non-residential/mixed-use tax accounts properties as at December 31, 2003.

Table 1:
Summary Analysis of Dollar Values and Number of Tax Accounts
with Credit Balances as at December 31, 2003.

Credit Ranges (\$)	Non Residential and Mixed-Use Properties		Residential		Totals	
	No. of Billings	Credit Balances	No. of Billings	Credit Balances	No. of Billings	Credit Balances
0 - \$100	2,964	\$75,115	33,679	\$507,735	36,643	\$582,850
\$100 – \$1,000	814	\$348,751	5,128	\$2,175,135	5,942	\$2,523,886
\$1,000 +	1,706	\$52,056,230	1,318	\$4,907,864	3,024	\$56,964,094
Grand Total	5,484	\$52,480,096	40,125	\$7,590,734	45,609	\$60,070,830

As identified in Table 1, of the 45,609 tax accounts that contain a credit balance, 80.4% or 36,643 accounts are identified as having a credit balance of less than \$100. Additionally, when accounting for the 5,128 residential tax accounts with a credit balance amount between \$100 and \$1,000, these combined segments represent 91.6% or 41,771 tax accounts, but only 4.6% of the total outstanding credit listing dollar amount.

The 2,520 non-residential (commercial, industrial and multi-residential) and mixed-use tax accounts with credit balances of \$100 and greater represent \$52.4 million, or 87.3% of the total outstanding credit listing. The 1,318 residential tax accounts with a dollar balance of \$1,000 or greater account for \$4.9 million, or 8.1% of the total credit listing amount.

In respect of the overall total dollar component, tax accounts with a credit balance of \$1,000 and greater represent 95% or \$57 million of the total credit listing of \$60,070,830. Conversely, this dollar segment represents only 6.7% or 3,024 accounts in relation to the total number of tax accounts impacted by a credit balance. The remaining 5% or \$3.07 million is attributed to tax accounts with a credit balance of less than \$1,000.

Recommended Changes to the Current Refund Process:

In an effort to improve customer service, while balancing the potential financial risks/liabilities associated with a change in policy and/or procedure for credit balances, the Finance Department, in consultation with Internal Audit and Legal Services, undertook a detailed review and analysis of the current practices, and number of tax accounts with accompanying dollar amounts relating to the tax refund process. In addition, Finance staff solicited and received input regarding the internal refund policies and the supporting legal opinions from the cities of Mississauga, Hamilton, Ottawa, London and Sudbury.

Legal Services has advised Finance that the language in the new *Municipal Act, 2001* (re: Section 341) authorized municipalities to refund overpayments of taxes associated with a successful assessment appeal to the current assessed owner.

Based on a review of the legislation, consultations with Legal Services, Internal Audit and other municipalities, as well as a review and analysis of the current procedures, statistical and financial data, Finance staff propose that the following changes be implemented to the tax refund process:

- (1) the processing of all credit balances/refunds resulting from a successful assessment appeal shall be refunded directly to whomever the Tribunal directs in its decision, and if no payee is named in the order, to the current assessed owner in accordance with Section 341 of the new *Municipal Act, 2001*, and where there has been a change in assessed owner(s) since the date the decision was released, a signed Indemnification Agreement will be required before any refund shall be made;
- (2) the processing of all credit balances of less than \$100 shall be applied as a credit to the tax account of the current assessed owner of said property. Amounts between \$15 and \$100 may be refunded to the current assessed owner by cheque, provided the City is in receipt of a signed written refund request;
- (3) the processing of residential tax credit balances between \$100 and \$1,000 shall be applied as a credit to the identified tax account or refunded to the current assessed owner upon receipt of a signed Indemnification Agreement and a signed written refund request; and
- (4) for all other credit balances, credit amounts shall be credited or refunded to the individual who made the overpayment, provided the City is in receipt of a written refund request signed by the claimant, together with an Indemnification Agreement in a form satisfactory to the City Solicitor and proof in a form satisfactory to the Director, Revenue Services or a designate, that the said claimant made the overpayment for which the refund is requested.

Legal Services recommends that an indemnification agreement be required for all refunds greater than \$100 and for assessment appeals, asserting that no one but the person receiving the refund has any right, title, interest or claim in the credit balance, and that the claimant agrees to indemnify the City of Toronto against all liabilities, claims, demands, costs or expenses resulting from the payment of the credit balance. This is recommended as the City has no way of knowing the contractual arrangements that were entered into between the current and previous owners.

Hence where a refund has been provided to a claimant, and the right to receive it is subsequently disputed by another party, the indemnification agreement is intended to insulate the City from costs it might otherwise incur if it were drawn into the dispute. A sample of the draft indemnification agreement is attached to this report as Appendix “C”.

Appendix “B” – *Refund/Credit Balance Operational Flow Chart* provides a visual overview of the recommended refund process.

The rationale behind the recommended changes to the processing of tax refunds is as follows.

(a) Credit Balances Resulting from a Successful Assessment Appeal:

Section 341 of the new *Municipal Act, 2001* supports a legal interpretation of the City’s obligation to refund the overpayment of taxes to the current assessed owner, as opposed to the person who paid, in the case of refunds arising from the settlement of assessment appeals under Sections 40, 39.1, 33 or 34 of the *Assessment Act*.

While subsection 37(6) of the *Assessment Act* still requires a municipality to refund taxes, subsection 341(2) of the *Municipal Act, 2001* requires the taxes to be “collected in accordance with the adjusted tax roll as if the adjustment had formed part of the original roll,” and then requires the municipality to “refund any overpayment.”

As advised by Legal Services, the new *Municipal Act* supports the legislative intention to require the municipality to refund in accordance with the adjusted tax roll, in the same manner as it collects taxes. As such, this would include providing refunds to the current assessed owner in the same way that taxes are collected from the current assessed owner. This strategy provides a clear opportunity to improve process efficiency when processing assessment appeals. In addition, as identified in recommendation one of this report, a signed letter of indemnification from the recipient taxpayer will be required where there has been a change in assessed owner(s) since the date the decision was released by the Tribunal for assessment appeal refunds.

This policy initiative for assessment appeals will lessen the margin of error in processing refunds, as it involves less investigation and calculation by City staff. This process also effectively removes the City from disputes between former and present property owners, as it leaves the issue of pro-rating refunds to the parties as part of their real estate transaction (vendor/purchaser agreement).

(b) Credit Balances less than \$100:

Accounts with credit balances less than \$100 comprise 80.4% (36,643 accounts) of all outstanding accounts with credit balances. The total credit balance on these accounts represents approximately \$580,000, or 1.0% of the total outstanding credit balance amount. Further analysis identified that approximately 10% of all refunds are disbursed to someone other than the current assessed property owner(s), therein only placing approximately \$58,000 at risk of being refunded incorrectly. In addition, the cost to taxpayers of

establishing proof of payment (e.g. bank statements, etc.) may, in many cases, approach the cost of the refund being provided. This recommendation, therefore, balances the customer service perspective with a manageable financial risk from the City's perspective.

Consequently, Finance staff will be able to allocate and focus their attention on the more complex and larger dollar credit balance amounts.

Where payable, credit balances of \$15 or less will be automatically applied as credits to the current tax account, rather than issued as refund cheques, due to the high costs of producing and mailing a cheque. Similarly, credit balances between \$15 and \$100 will also be automatically applied as credits to the current tax account, unless an owner has requested in writing that a refund cheque be issued for a credit balance. Currently, there are in excess of 24,000 tax accounts with credit balances of \$15 or less.

(c) Residential Credit Balances more than \$100 but less than \$1,000:

These accounts represent 5,128 tax accounts (11.3% of the total listing), accounting for approximately \$2.2 million or 3.6% of the total outstanding credit balances. The statistical analysis from above identifies that only 10% of this category may result in refunds not being refunded to the current assessed owner. As such, approximately \$0.22 million or only 0.4% of the total credit balance amount is at risk of being refunded in error if refunds are provided to the current assessed owner.

The above two categories combined represent a substantive 91.7% or 41,771 of the total 45,609 tax accounts with a credit balance, of which approximately \$0.28 million, or only 0.5% of the total credit listing, may be refunded to the current assessed owner in error. Further, when an error has been identified, staff will undertake the required action to correct the error on a case-by-case basis.

In consultation with the Internal Auditor and Legal Services, it is felt that these recommendations represent a balanced approach that considers the ease of a taxpayer attaining outstanding credit balances, while maintaining the integrity of the financial position of the City and fulfilling statutory legal requirements. As a result, Finance staff will be able to address the remaining 3,838 tax accounts, representing \$57.3 million or 95.4% of the total credit balance amounts.

(d) Non-Residential Credit Balances more than \$100 and Residential Credit Balances more than \$1,000:

In all other situations, credit balances shall be refunded to the individual who made the overpayment, provided acceptable proof of payment is received, (e.g., bank statements or cancelled cheques, and/or a statement of adjustments attesting to the source of and entitlement to the refund payment from a lawyer qualified to practice law in Ontario), together with a signed indemnification agreement.

As a result of the substantial dollar amount associated with these 3,838 tax accounts, and due to the often complex nature of tax payments on business properties, and the potential for multiple ownership changes common among the non-residential segment, Internal Audit and

Finance staff agree that more stringent policy standards and proof of payment requisites are needed to ensure that credit refunds are provided to the party that made the payment. Additionally, it is assumed that, in the case of business tax accounts, it is often easier for businesses to furnish adequate proof of payments, through their own bank statements or financial records.

For these 3,838 accounts, the non-residential segment represents 2,520 tax accounts, totalling approximately \$52.4 million (87.3%), while the residential credit balances in excess of \$1,000 account for the remaining 1,318 tax accounts, totalling approximately \$4.9 million (8.1%). On average within this segment, each tax account would represent a credit balance refund of approximately \$14,930 per account.

The implementation of the recommendations in this report represents a significant departure from past practices followed by any of the former municipalities and the City of Toronto. Therefore, the City must impress upon property owners that it is their responsibility when selling a property to make arrangements regarding appeals or any other overpayments at or prior to the time of closing of the real estate transaction. The City's responsibility continues to be to the tax account for the property, as the tax responsibility runs with the land, regardless of ownership. To facilitate the transition to the new refund policy, an extensive communication strategy will be developed to inform taxpayers, legal firms and financial institutions of the new operational procedures for refunds.

On the advisement of the Internal Auditor, Finance staff will monitor and review the new operational processes regarding credit balances, to ensure optimal customer service and protection of the financial integrity of the overall process.

Conclusions:

This report recommends the adoption and implementation of new refund policies and operational processes for assessment related appeals and credit balances, which will allow Finance staff to improve customer service and realize operational efficiencies within the refund process. The recommended procedures will see credits of \$1,000 and less refunded to the current owners of residential properties upon request. Larger refund amounts, and non-residential tax accounts will continue to require some form of proof of payment, as a means of ensuring that refunds and/or

credits are provided to the party having made the payment. The recommended procedures are intended to balance the customer service perspective with a manageable financial risk from the City's perspective.

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List of Attachments:

Appendix A: *June 16, 2003 Communication from Councillor Moscoe*

Appendix B: *Refund/Credit Balance Operational Flow Chart*

Appendix C: *Draft Indemnification Agreement*