THE TIFF WITH TIEG:

AN EVALUATION OF THE CITY OF TORONTO'S IMIT PROGRAM

by

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B.A., York University, 2017

A Major Research Paper

presented to Ryerson University

in partial fulfillment of the requirements for the degree of

Master of Planning
in
Urban Development

Toronto, Ontario, Canada, 2019

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ABSTRACT

Facing an increasingly integrated and competitive global economy, local governments have developed property tax incentive programs to entice businesses to build and locate domestically. This paper offers an account of how one specific property tax incentive program – the City of Toronto's Imagination, Manufacturing, Innovation and Technology (IMIT) program – came into existence and how it has evolved into the present day. An evaluation criteria analysis that builds on Hemson Consulting's 2017 review of IMIT follows. A review of literature and policy culminates in a list of recommendations for the City to consider as it strives to achieve its economic development objectives.

Key words: property tax, incentive, economic development, employment

Acknowledgements

I would like to first and foremost thank my MRP supervisor, Professor David Amborski, for his support throughout the ideation, writing and editing processes. A special thank you to Ian Andres for agreeing to be my Second Reader and for offering insightful comments that added great value to my paper.

I am grateful to Rebecca Condon at the City of Toronto for providing me with much-needed context about the IMIT program and helping to fill in the gaps in my understanding of the program.

My decision to write about this topic comes from a desire to see my hometown Scarborough develop into a thriving live, work, play community. I hope City staff will thoughtfully consider the recommendations put forward in this report.

A final thank you to my parents for letting me live at home free of charge throughout my Master program and for their ongoing support.

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1. Introduction

1.1. The Challenge for Contemporary Municipalities

When Amazon Inc. – the trillion-dollar internet retailer headquartered in Seattle – announced in 2017 that it was looking for another city to host its second headquarters ("HQ2"), municipalities across the continent began jockeying for position. The lure of a promised 50,000 new full-time jobs and over $5 billion in capital expenditures was too great to resist. In addition to highlighting their region's unique strengths and opportunities, many governments turned to a crasser alternative to make their case – money, specifically direct subsidies and tax incentives. Maryland and New Jersey each offered $8.5 billion and $7 billion packages, respectively (McCartney, 2018). Arlington County and the Commonwealth of Virginia, successful in their collective bid, teamed up to offer Amazon $573 million (Nickelsburg, 2018). New York State, in support of New York City's initially successful bid, offered $1.5 billion in tax incentives in addition to hundreds of millions more in investment subsidies (Nickelsburg, 2018). In an interesting twist, Amazon stated only weeks after its announcement of the winners that it would not be moving forward with plans for the New York City campus. The company cited political pushback from state and local elected officials as the reason.

The Amazon bid renewed an intense debate that has been happening for decades. Are these extravagant tax incentive packages for wealthy firms justifiable? What prompts cash-strapped municipal councils to forgo massive amounts of tax revenue that could instead be used to help solve a myriad of urban problems?

Falling transportation and communication costs spurred by technological innovation have eased the friction of distance and made other determinants – including taxes – more important in the corporate site selection process. This led to the erosion of many central cities as the traditional advantages associated with geographic concentration diminished. In order to woo firms and employment back, central cities offered economic development incentives, including tax-based incentives (Kenyon et al., 2012). Markusen and Nesse (2007) point to two additional factors that gave rise the tax incentive as a municipal economic development tool: the rise of site location consultancy as a major service industry and the devolution of economic development responsibilities from national to subnational governments. In short, increased economic competitiveness in a highly inter-connected world of mobile firms has led to increased use of tax incentives by subnational governments.

In the Amazon HQ2 bid process, Toronto distinguished itself for its refusal to offer tax incentives to the company. “Others may provide large subsidies and tax breaks, but like the Province of Ontario, we in the Toronto Region don’t want to play that game and frankly we feel we don’t need to play that game,” stated economic development group Toronto Global’s CEO Toby Lennox (Boisvert, 2017). However, this hypocritically ignores the more than half a billion dollars in property tax incentives that the City of Toronto has provided to corporate entities through its Imagination, Manufacturing, Innovation and Technology (IMIT) program.

1.2. IMIT Program Overview

Prior to the recession of the early 1990s, non-residential construction within Toronto was abundant and employment was at an all-time high of 1.35 million jobs (City of Toronto, 2008b). However from 2000 to 2006, employment within the City decreased by 1.6 percent, even while job creation in the rest of the region *grew* by 27.8 percent (Mayor's Economic Competitiveness Advisory Committee, 2008). An abundance of easy-to-develop employment lands and lower industrial and commercial tax rates in the outer suburbs, as well as the lucrative market for residential development, had the combined effect of dampening market interest in new industrial and smaller scale office projects within Toronto (Mayor's Economic Competitiveness Advisory Committee, 2008). From 1995 to 2007, the level of expenditure on buildings in the region outstripped the City by an average of 34 percent (City of Toronto, 2008a).

Created in 2008, IMIT aims to support new building construction and/or expansion in targeted economic sectors. The summary of the program that follows is taken from Hemson Consulting (2017) and City of Toronto (2018a).

In its most recent iteration, the program targets the following sectors and uses:

Sectors

- Biomedical Operations
- Creative Operations
- Financial Services
- Information and Communications Technology
- Manufacturing
- Tourism Attractions

Uses

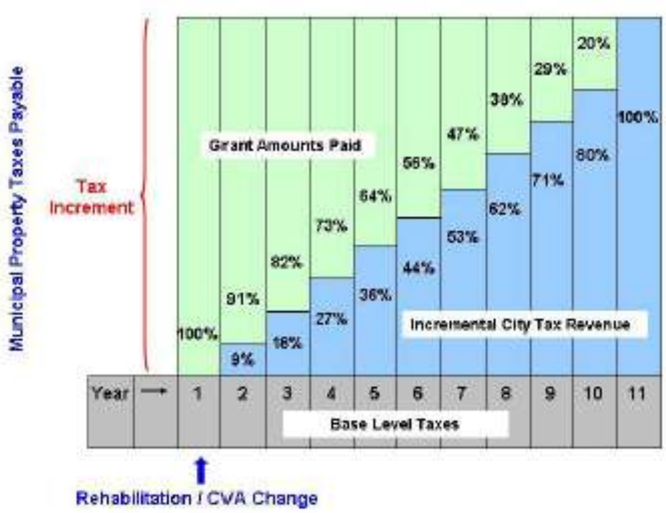
- Broadcasting
- Call Centres

- Computer Systems Design and Services
- Convergence Centres
- Corporate Office
- Corporate Headquarters
- Film Studio Complex
- Food and Beverage Wholesaling
- Office Building
- Incubators
- Information Services and Data Processing
- Scientific Research and Development
- Software Development
- Transformative Project

Eligible projects must have a minimum construction value of $3 million and must increase the gross floor area (GFA) of eligible sectors or uses by at least 500 square metres.

The incentive provided through the program is a partial property tax abatement, provided in the form of tax increment equivalent grants (TIEGs) over ten years, with 60 percent of the municipal tax increment for eligible uses over that period returned to the property owner. Figure 1 provides a breakdown of the TIEG structure.

Figure 1 - IMIT Program TIEG Structure



Retrieved from Hemson Consulting Ltd. (2017)

The program also includes a Brownfield Remediation Tax Assistance (BRTA) component, which provides a cancellation of taxes equivalent to 70 percent of the municipal tax increment over a ten-year period for the remediation of contaminated land associated with eligible uses.

1.3. Purpose and Objectives

The purpose of this report is to conduct a review of the City of Toronto's IMIT program based on an evaluative criteria analysis and on the basis of that analysis, develop program recommendations. Given that Hemson Consulting produced a formative evaluation of the IMIT program as recently as 2017, this paper will not attempt to repeat their work. Rather, this paper will apply a more comprehensive list of criteria in evaluating the program.

In order to achieve these objectives, the report will investigate the following questions:

- What factors must be considered when seeking to evaluate the IMIT program?
- Is the property tax abatement an effective and equitable tool for achieving the City's economic development objectives?
- How can the IMIT program be amended to better achieve the City's economic development objectives?

In addressing these questions this report will provide valuable insights to Toronto's municipal officials, development community and broader citizenry about a program of great consequence to the municipal budget and the Toronto taxpayer. This report also offers itself as a useful resource for municipal officials in other jurisdictions with comparable legislation that are considering implementing their own property tax incentive programs.

2. Methodology

The analysis within this paper is informed by four parts: an academic literature review; an interview with a City of Toronto staff member; a review of City documents, reports and bylaws and Council proceedings pertaining to the IMIT program; and a review of Hemson Consulting's 2017 study of the IMIT program. The four portions of this analysis will culminate in a set of recommendations for the City to consider as it relates to the structure of the IMIT program.

The literature review portion will cover a brief history of property taxation in Ontario, a review of corporate site selection factors and a summary of studies and meta-analyses that have been conducted of tax incentive programs across the United States. Due to their status as "creatures of the province", Ontarian municipalities have only recently received the legal authority to enact tax incentive programs and still lack many of the tools available to their US counterparts.

In addition to an evaluation of the IMIT program as it is today, this paper attempts to retrace the history of the program, specifically the three iterations of the program and the rationale behind the changes that were made during each review. This is accomplished by comparing the enabling bylaws (2008, 2012 and 2018) against one another and analyzing staff reports. The interview with a senior ED&C staff member helped to provide more detailed context to information gleaned from the bylaws and staff reports.

3. Literature Review

3.1. Property Taxation in Ontario

According to Kenyon et al. (2012), the rationale for levying property taxes on businesses is threefold. Firstly, it is to recover the cost of government services provided. This includes transportation infrastructure, water and sewage systems, the court system, policing and educational services, among other things. Secondly, it is to generate revenue for local governments. In 2009, businesses contributed 58 percent of all property taxes raised in the United States. Property taxes in turn constituted 40 percent of all state and local taxes paid by businesses. Thirdly, property taxes are levied on businesses in order to counteract the regressive elements of the tax system, such as the sales tax. Business property taxes are conceived of as a tax on capital, which is disproportionately held by higher-income individuals. Thus, this form of taxation can be seen as adding progressivity to the tax system (Kenyon et al., 2012).

The legislative ability for Ontario municipalities to levy property taxes was first enshrined in the *Municipal Act* of 1849. Property taxes constituted a lien on land, which in the event of a default could be sold for taxes. An income component was added to the definition of personal property in 1866, but was removed in 1904. The 1904 reform also introduced a graduated business tax based on a specified percentage of assessment, depending on the activity occurring on the property (Hemson Consulting Ltd., 2012).

In 1967, as part of a review of taxation in Ontario, the Smith Committee released a report recommending that real property be assessed according to market value in order to eradicate noted inequities between individual taxpayers, classes of taxpayers and municipalities. However, sudden reform would have resulted in significant shifts in the tax burden. A thirty year effort ensued that attempted to achieve reform while mitigating associated harms (Hemson Consulting Ltd., 2012).

In 1995, the Progressive Conservative government of Mike Harris was elected to power in Ontario on a platform that called for more bureaucratic efficiency. The Harris government undertook a review of provincial-municipal service delivery arrangements with the aim of taking direct control over education. In exchange for relieving municipalities of 50 percent of school funding costs, the Province downloaded costly new responsibilities to local governments. The business tax was abolished, compensated for with higher property tax rates on commercial and industrial properties. The net result was that municipalities became much more dependent on property taxes and user fees to fund the cost of new services as provincial transfer payments dwindled (Hemson Consulting Ltd., 2012).

The Harris reforms made property taxation the backbone of municipal finance in Ontario. There are more than 4.7 million properties within the province, which in 2009 were valued at more than $1.7 trillion (Hemson Consulting Ltd., 2012). In 2008, almost 70 percent of Ontario municipalities' own-source revenue was generated through taxation of these properties (Hemson Consulting Ltd., 2012). This sits in contrast to the United States, where local governments have access to a plethora of revenue tools not enjoyed by their Canadian counterparts. The sales tax, for instance, comprised 14.3 percent of own-source revenues for U.S. municipalities in 2007 (Kenyon et al., 2012).

3.2. Use of Property Tax Abatements

The use of property tax incentives is relatively new to Ontario, given it was only recently that Ontarian municipalities were permitted to offer financial inducements to new businesses (Slack, 2008).

The first recorded use of commercial property tax abatements in the United States is from 1640 in what would become the state of Connecticut. Throughout the 1800s, eastern states granted property tax exemptions in order to spur manufacturing growth and generate employment opportunities for the poor. Following the American Civil War, abatements became popular with Southern States looking to draw industry away from the Midwest and Northeast. State and local governments turned to similar programs again after the Second World War in order to generate well-paying employment opportunities for returning veterans and the oncoming generation of baby boomers (Wassmer, 2007). Between 1964 and 1979, the number of states allowing property tax abatements increased from 15 to 31. By 2010, 37 states had legalized their use (Kenyon et al., 2012).

This growth in the use of tax incentives to attract economic growth can be attributed to a number of causes. As a result of technological innovation, transportation and communication costs have declined dramatically and supply chain management has improved. This has made firms more mobile and as a result has made firms more sensitive to costs that vary by location, such as taxes. As firms have taken flight to suburban locations, inner cities have felt pressure to respond with tax incentives. Tax incentives – as opposed to across-the-board tax cuts and direct expenditure on economic development – are politically appealing because their cost is less transparent and unlike the latter, are not subject to highly-visible annual appropriations. Once one municipality within a region introduces tax incentives, neighbouring municipalities feel pressure to respond in kind in order to remain competitive. The more that tax incentives are used, the more firms come to expect them which creates a vicious cycle whereby incentives become the norm rather than the exception (Kenyon et al., 2012).

3.3. Site Selection Process and Factors

In assessing the impact of varying property tax rates and incentives on economic development, it is necessary to consider the factors that are proven to influence the corporate site selection process.

Corporate site selection at its simplest can be viewed as a two-step process. A firm first chooses a metropolitan area and then chooses a particular site within that region (Kenyon et al., 2012). Fantus Consulting, an economic development consulting firm based in Los Angeles, uses a slightly more nuanced and widely used three-step site selection process.

The first stage compares wage differentials, transportation variables and project-specific essentials (e.g. proximity to engineering school) across an array of regions and narrows these down to a single broad region, several states or several counties. Taxes are only considered at a high level. The second stage involves modeling operating costs for the specific project in an array of jurisdictions, with the intent of further refining the list to three to five communities. Of firms that used Fantus Consulting for site selection from 1992 to 1997, input cost categories were weighted as follows: labour

(36 percent); transportation (35 percent); utilities (17 percent); occupancy (8 percent); and taxes (4 percent) (Kenyon et al, 2012). Property taxes only account for 1 percent of total costs for the U.S. manufacturing sector; as Kenyon et al. (2012) point out, "large variations will have little effect on firm location decisions if a cost factor accounts for a small share of total costs" (p. 23).

Only in the third stage, when choosing a specific site, are all taxes and incentives considered in full. It is only in a relatively autonomous geographic region that tax differentials have the potential to sway a firm's location decision because most significant input costs are comparatively uniform at that scale (Kenyon et al., 2012). The literature supports the notion that local property taxation is not a statistically significant factor in the inter-metropolitan location decisions of mobile firms (Kitchen, 1985; Ontario Fair Tax Commission, 1992; Bartik 1991).

The Boyd Company, another firm that provides site selection counsel to American corporations and is one of that nation's premier authorities in comparative business cost analysis, conducted a study in 2016 that compares the cost of operating a typical food processing plant in 24 regions of the U.S. and Canada. They make note of five factors that are heavily influencing site selection decisions in the food manufacturing sector.

Firstly, the U.S. Food Safety and Modernization Act has mandated upgrades to food processing plants that will add to firms' operating costs. Secondly, the presence of drought throughout California and the western U.S. has made water availability and cost an important factor. Upstate New York and Eastern Ontario are noted for being waterrich locations. Thirdly, access to Asia' burgeoning middle class consumer market is a prime consideration. Principal John Boyd makes special note of Canada for its participation in double the number of trade agreements as the U.S., including the Trans Pacific Partnership.

The fourth factor includes a number of advantageous conditions which make Canada (specifically Eastern Ontario) a profitable place to conduct business. This includes a favourable exchange rate, low world-market sugar prices, low land costs, absence of development fees and lower benefit costs owing to Canada's public health insurance plan. Boyd considers the Ontario government's Jobs and Prosperity Fund – introduced in 2015 – to be "one of the most extensive and best funded incentive programs in North America" (Boyd, 2016). Contained within the Fund is a Food and Beverage Growth Fund, which provides financing for investments that create sustainable jobs, enhance innovation and productivity, or strengthen supply chains in the food, beverage and bioproduct processing sectors (Ontario, n.d.). Of the 24 regions included in the Boyd Company's analysis, Eastern Ontario was found to be the lowest-cost location.

Finally, firms in the food manufacturing sector have been faced with the challenge of finding skilled labour that can operate high-tech equipment on the production floor as well as undertake quality control research and testing. Consequently, locations that offer colleges with strong programs in food technology are given special consideration. Belleville – with its presence of Loyalist College – is noted for this reason.

Studies do suggest that property tax rates hold the potential to sway locational decision-making at the intra-metropolitan level (Wasylenko, 1980; Fox, 1981; Charney, 1983; McGuire, 1985; Walker and Greenstreet, 1991). Bartik (1991) and Wasylenko (1997) summarize the results of roughly 90 studies that used regression analysis to estimate the effect of state and local taxes on economic activity.Their results show that differences in taxes within a given region have a five to ten times greater impact on economic activity than differences across regions (Kenyon et al. 2012).

Wasylenko (1980) examined the relocation decisions of 359 firms that moved from Milwaukee to one of its 59 suburban municipalities between 1964 and 1974. The effect of property taxation on locational decision-making for firms in the manufacturing and wholesale trade sectors was found to be statistically significant. Conversely, for firms in the construction, retail trade, finance and service sectors, the impact of property taxes was not statistically significant. Walker and Greenstreet (1991) discovered that property taxes exert a significant negative effect of location choices of manufacturing plants in the Appalachian region. In the Minneapolis-St. Paul metropolitan region, property taxes were found to have a statistically significant impact on the location of business building permits. A 1 percent increase in tax rates correlated with a 2 percent decline in location activity (McGuire, 1985).

The findings of Bollinger and Ihlanfeldt (2003) appear to contradict these findings. Property tax rate did not register as exerting a statistically significant effect on change in intra-metropolitan employment share for Atlanta region municipalities. However, the authors point out that "intertemporal movements in tax rates are highly correlated across jurisdictions over the years covered in our panel, making it difficult to isolate their effect" (408).

3.4. Property Tax Abatement Programs: A Critique

Property tax abatement programs allow partial or full reduction in property tax liability for certain manufacturing, commercial or retail parcels. Abatement can come in various forms, including exemption, tax credit, freeze, etc. The most common duration for a tax abatement is 10 years. In a study of abatement programs in the U.S., Kenyon et al. (2012) found that nearly half of them contained no limiting provisions; 35 percent allow for termination of tax incentives if certain criteria are not met; 18 percent included "clawbacks" that require firms to pay back some portion of the abatement; and 7 percent have a program end date.

The literature is overall not favourable to the use of tax abatements. Abatement proponents argue that despite the short-term foregone revenue, abatements actually improve the fiscal health of municipalities because they attract eventual tax-paying firms that otherwise would not have located there. However, as aptly stated by Nunn (1994) "the success of tax abatement decisions is difficult to assess because there is no practical way of knowing whether tax abatements were the real cause of a business location decision" (576). McHone (1984) finds only a weak relationship between differences in employment growth and industrial development incentive advantages that a county has over other parts of the metropolitan area. Wassmer (1994) determines that of 31 municipalities in metropolitan Detroit, in only 5 of them was the commercial or industrial abatement found to exert a statistically significant positive effect on the long-term growth trend.

Even assuming increased economic activity is attributable to tax abatement, this surge in activity does not necessarily translate into tax revenue growth for the municipality. In its audit of the Department of Urban Development's urban development action grant (UDAG) program, the U.S. General Accounting Office (GAO) found that though total reported private investment exceeded expectations by 21.5 percent, this increase did not translate into improvements in the local tax base as tax revenues from the projects fell short of expectations by 31 percent (Nunn, 1994). Furthermore, there is a risk that new firms will compete directly with existing firms. Any net economic benefits gleaned through abatements will in this case be diminished as profits of new firms displace the profits of existing ones (Kenyon et al., 2012).

One strain of thought argues conversely that new firms will improve the business environment for existing and future businesses through the creation of agglomeration economies, wherein all firms experience productivity increases as the number or size of geographically concentrated firms increases. This argument is taken up in Garcia-Mila et al. (2002). If the optimal corporate tax rate is set at the marginal benefit to firms from their use of public goods and services, as is argued in Oates and Schwab (1988), this does not take into account the positive spillover effects of agglomeration economies that result when a new firm locates within a jurisdiction. When these spillovers are accounted for, the optimal tax rate decreases. However rather than supporting an across-the-board tax cut, Garcia-Mila et al. (2002) favour selective tax breaks in recognition of the fact that cities are each at various stages of economic production and will want to attract specific types of firms to the neglect of others:

> Existing business services firms are likely to benefit more than existing manufacturing firms from the spillovers of human capital and knowledge associated with a newly relocating corporate headquarters firm. Thus it may be optimal for a city with a base of business services firms to offer a tax incentive to a relocating headquarters firm, whereas it may not be in the best interests of a city with a base of traditional manufacturing to do so (107).

In the same way, firms may desire particular locations over others. It helps the municipality to achieve the greatest benefit for itself when it can charge differential taxes depending on the firm and its eagerness (or lack thereof) to locate there (Glaeser, 2002). Property tax abatements offer a de facto means of doing so.

One metric that is used by economic development officials to assess requests for abatement is the number of jobs created. This is not an exact science however, and there is evidence of significant variations between projected jobs and actual jobs. In its audit of the UDAG program, the U.S. GAO found that projected jobs exceeded actual jobs in more than two-thirds of 1,116 completed projects (Nunn, 1994). Moreover, it cannot be assumed that newly created jobs will accrue to local residents. An analysis of 18 studies in Bartik (1993) concludes that 60 to 90 percent of jobs created by employment programs go to in-migrants or unintended beneficiaries.

Gabe and Bell (2004) note that businesses favour municipalities that spend high amounts on public goods and services, even when said spending is accompanied by higher property tax rates. When local governments reduce public expenditure as a result of tax abatement provision, it can actually dissuade firms from locating there. The results of Bollinger and Ihlanfeldt (2003) corroborate this claim. Among municipalities in Atlanta's metropolitan region, higher expenditures in fire safety, road improvements and parks were found to increase intra-metropolitan employment share.

Abatements create concerns around corruption and inequity. When tax incentives are awarded on a discretionary basis in ways that are at times not transparent or lack a clear economic justification, it can erode public trust in political and bureaucratic institutions (Kenyon et al., 2012). Tax abatements can create further inequities as they may involve a shifting of the tax burden onto unabated properties (Mullen, 1990; Slack, 2008). This stands in direct contradiction to the principle that growth should pay for growth. An overall tax rate reduction within a jurisdiction is seen as more transparent and equitable, and has been shown to increase business activity more consistently than the selective use of abatements to specific firms (Slack, 2008). Wassmer (2009) notes an elasticity of -2.0 between property taxes and economic activity (meaning that a 10 percent reduction in property taxes is associated with a 20 percent increase in economic activity). Wasylenko (1997) summarizes the case as follows:

> When the business climate of a state becomes so problematic that tax laws need to be changed routinely to attract businesses, the practice may be a symptom of problems with the tax system itself and a signal that systematic tax reform might be a more useful approach. In effect, tax reform treats existing and new firms equally, and responsible reform will also systematically account for any tax revenue lost due to reform (p.49).

Tax abatements can distort business expectations, leading to long term negative impacts on municipal fiscal health. In 112 Detroit-area communities, the average percentage of property value granted an abatement was 2 percent in 1977. This had grown to 35 percent by 1992. Anderson and Wassmer (2000) argue that the reason for this growth is that abatements were losing their impact after other municipalities began to offer them and firms began to expect them. Indeed, abatements appear more successful when only one municipality within a metropolitan region is offering them (Slack, 2008).

4. Legislative Underpinnings and Policy Rationale

Section 28 of the *Planning Act* provides the legal foundation and parameters for community improvement planning in Ontario. Under Section 28(2), the council of any municipality with an official plan containing community improvement policies may pass a bylaw to designate the entire municipality or any sub-area within it as a community improvement project area (CIPA). A CIPA is defined as:

> a municipality or an area within a municipality, the community improvement of which in the opinion of the council is desirable because of age, dilapidation, overcrowding, faulty arrangement, unsustainability of buildings or for any other environmental, social or community economic development reason.

"Community improvement" is defined broadly as

> the planning or replanning, design or redesign, resubdivision, clearance, development or redevelopment, construction, reconstruction and rehabilitation, improvement of energy efficiency, or any of them, of a community improvement project area, and the provision of such residential, commercial, industrial, public, recreational, institutional, religious, charitable or other uses, buildings, structures, works, improvements or facilities, or spaces therefor, as may be appropriate or necessary.

Once such a bylaw has been passed, council may prepare a community improvement plan (CIP) for the CIPA. For the purposes of implementing the CIP, Section 28(7) permits the municipality to issue grants or loans to registered owners, assessed owners and tenants of lands and buildings within the CIPA to help cover eligible costs, defined broadly as,

> costs related to environmental site assessment, environmental remediation, development, redevelopment, construction and reconstruction of lands and buildings for rehabilitation purposes or for the provision of energy efficient uses, buildings, structures, works improvements or facilities.

Though Section 106(1) of the *Municipal Act* prohibits municipalities from engaging in bonusing, Section 106(3) of the *Municipal Act* exempts from this requirement municipalities exercising their authority to implement a CIP under Section 28(7) of the *Planning Act*. Likewise, Section 82 of the *City of Toronto Act, 2006* prohibits the City from assisting any manufacturing business or other industrial or commercial enterprise financially, but provides an exception when financial incentives are granted pursuant to the *Planning Act*'s Community Improvement provisions.

Section 5.2.2 of the City of Toronto Official Plan (2006) states that

> Community Improvement Project Areas will be designated by by-law, and CIPs will be prepared to promote the maintenance, rehabilitation, revitalization and/or conservation of selected lands, building and communities facing challenges of transition, deficiency or deterioration or for any other environmental, social or community economic development reason.

As such in May 2008, Toronto City Council adopted CIP bylaws designating a City-wide CIPA, Waterfront CIPA and South of Eastern Employment District CIPA. Adoption of the bylaws under Section 28 of the *Planning Act* permitted the issuance of TIEGs to property owners through the IMIT program.

The objectives of the CIPs Council has adopted align with several municipal and provincial policies, including:

- Creating a strong and competitive economy with a vital downtown that creates and sustains well-paid, stable, safe and fulfilling employment opportunities for all Torontonians (OP p1-2).

- Creating a variety of jobs available to people with a range of education and abilities that creates and sustains well-paid, stable, safe and fulfilling employment opportunities for all Torontonians (OP p1-3).
- Creating diverse employment areas can adapt to changing economic trends and are poised to capture new business opportunities (OP p1-3).
- Encouraging the establishment of key clusters of economic activity with significant value-added employment and assessment (OP, Sec. 4.6.6 b).
- Meeting employment targets as outlined in the Growth Plan for the Greater Golden Horseshoe (2017) and Toronto's Official Plan.
- Provincial Policy Statement (2014) section 1.1.3.3, which states that

  Planning authorities shall identify appropriate locations and promote opportunities for intensification and redevelopment where this can be accommodated taking into account existing building stock or areas, including brownfield sites, and the availability of suitable existing or planned infrastructure and public service facilities required to accommodate projected needs.
- Provincial Policy Statement (2014) section 1.3.1, which states that

  Planning authorities shall promote economic development and competitiveness by:

  a) providing for an appropriate mix and range of employment and institutional uses to meet long-term needs;
  b) providing opportunities for a diversified economic base, including maintaining a range and choice of suitable sites for employment uses

which support a wide range of economic activities and ancillary uses, and take into account the needs of existing and future businesses;

c) encouraging compact, mixed-use development that incorporates compatible employment uses to support liveable and resilient communities; and

d) ensuring the necessary infrastructure is provided to support current and projected needs.

5. IMIT Program Evolution

The IMIT program is now in its eleventh year in force and is in its third iteration, following program reviews in 2012 and 2017. Appendix A provides a summary of the distinctions between the three iterations.

5.1. By-law Nos. 516-2008, 517-2008, 518-2008

Council in December 2007 approved in principle the introduction of a City-Wide Financial Incentives Program in order to stimulate investment in the industrial and commercial sectors of the city.

Staff tabled an implementation plan in April 2008. Using 2001 Census data, they identified the Location Quotient – a measure of the concentration of business activity compared to the population base – of various economic sectors within the City of Toronto. Staff recommended that the primary objective of the new financial incentive program should be to help accelerate growth in the economic sectors with the highest Location Quotients (i.e. the sectors that Toronto has a competitive advantage in relative to the rest of Canada). Additional criteria for eligible sectors included ones that:

- generally produced goods and services traded outside the region so as to provide new economic wealth;
- generally provide higher wages (50 percent to 100+ percent higher than retail);
- have international linkages; and
- create higher than average employment densities (City of Toronto, 2008a).

The chosen sectors were: Manufacturing (including accessory office, warehousing operations and energy/cogeneration operations), Information and Communications Technology (including computer systems design and services, information services and data processing, and software development), Environmental Industries, Biomedical

Operations, Creative Industries, Tourism Attractions and Transformative Projects (City of Toronto, 2008a).

The implementation plan notes that "the use of incentives to attract investment around the world is a common and accepted practice" and that "the availability of incentives will keep Toronto on the list of potential international sites for a new facility" (City of Toronto, 2008a, p.19-20). However it is acknowledged that in order to avoid a "race to the bottom" scenario whereby Toronto and neighbouring municipalities engage in an escalating war of incentives to the detriment of the collective regional economy, a financial incentive program should have incentives that:

- are made available only to specific targeted industries;
- are time limited;
- have clearly designed and measurable expectations;
- have mandated performance targets;
- have clawbacks for non-performance (City of Toronto, 2008a).

By-law Nos. 516-2008, 517-2008 and 518-2008 were enacted on May 27, 2008. They created a City-wide CIPA, South of Eastern CIPA and Waterfront CIPA, respectively.

A unique set of circumstances led to the designations of "Waterfront" and "South of Eastern" as their own CIPAs. In 2001, the City of Toronto in partnership with the provincial and federal governments established the Toronto Waterfront Revitalization Corporation (TWRC), better known as Waterfront Toronto. The new entity's mandate was to transform 800 hectares of brownfield lands along Toronto's Waterfront into a set of sustainable, mixed-use communities and vibrant public spaces. There was also a distinct emphasis on leveraging this opportunity to be innovative and to deliver economic benefits that would allow Toronto to compete internationally for jobs, talent and investment (Waterfront Toronto, n.d.).

However there were significant challenges to private investment in the Waterfront. Chief among them was the lack of amenities (such as restaurants and stores for workers, parks and business services), limited access to the subway and GO transit system and market rents that may not have been high enough to support the development costs of new buildings (Hemson Consulting Ltd., 2005). A report by Hemson Consulting recommended that the administering of grants through a CIP could be an effective tool to provide direct assistance to developers.

In April 2003, Council had approved the Central Waterfront Secondary Plan which subdivided the Waterfront into a set of precincts. In order to pave the way towards a development grant program, Council approved By-law No. 1027-2006 which established the East Bayfront, West Don Lands, Port Lands and South of Eastern CIPA. Two years later when the IMIT Development Grant program was formally created, it was decided that parts of the East Bayfront, West Don Lands and Port Lands precincts would form their own "Waterfront" CIPA and the South of Eastern precinct would form a separate CIPA. Council had at that point recently adopted a Secondary Plan for the South of Eastern Employment District. A separate CIPA was seen at the best way to guarantee alignment between the development grant program and Secondary Plan policies and objectives (City of Toronto, 2008). Table 1 highlights the key differences between the three bylaws in terms of uses permitted in each.

Table 1 – IMIT CIPs Sector/Use Differences

	City-wide 516-2008	South of Eastern 517-2008	Waterfront 518-2008 (Port Lands, West Don Lands, East Bayfront)
Business and Financial Services	No	No	West Don Lands, East Bayfront
Manufacturing	Yes	Yes	Port Lands
General Office	No	Yes	West Don Lands, East Bayfront
Film Studios	No-except Wallace-Junction	Yes	Port Lands
Colleges- Targeted Sectors	No	No	West Don Lands, East Bayfront
Tourism Attractions	Yes	No	West Don Lands, East Bayfront
Transformative Projects	Yes	No	No

Retrieved from City of Toronto (2012a)

5.2. By-law Nos. 1323-2012, 1324-2012, 1325-2012

The 2012 program review was conducted by staff within the City of Toronto's Economic Development and Culture (ED&C) Division using an external review panel of stakeholders. In its first four years, the IMIT program resulted in approved funding for 13 projects totalling 3.86 million square metres of new gross floor area, $800 million in construction investment and nearly 13,000 jobs created or retained (City of Toronto, 2012a). The total cost to the City in terms of foregone tax revenue was calculated to be $95.2 million. Therefore the subsidy per job equated to approximately $7,323.

25 applications were submitted in total, with 7 having been found ineligible, been withdrawn or having become inactive. The remaining 5 applications were still in the approval process at the time of report publication. 5 applications qualified for BRTA and

incurred or were projected to incur an estimated $17 million in qualified remediation expenses.

Recommendations were put forth by both the external review panel and City staff for Council consideration. Table 2 recounts each recommendation as well as its respective status in the 2012 City-wide CIP By-law.

Table 2 - Results of 2012 Program Review

Recommendation	Status in Bylaw 1323-2012
1. Renew the IMIT program	Addressed as recommended.
2. Removing the expiry date from the CIPs	Addressed as recommended. The 2008 CIP bylaws contained a provision whereby the bylaws would expire in five years after their coming into full force unless Council amended the bylaws to revise the expiry date or delete the provision. Council elected to delete the provision.
3. Setting for the next program review to be four years thereafter, with such review including a recommendation as to whether the IMIT program should continue	Addressed as recommended.
4. Increasing the incentive level for eligible applicants constructing new buildings or substantially renovating existing buildings in Employment Districts and other designated Employment Areas by i. increasing the TIEG amount to 70% of the cumulative municipal tax increment over ten year period; or ii. increasing the total amount of assistance to 77% of the municipal tax increment over a maximum 12 year period when development grants are provided in conjunction with BRTA	Addressed as recommended.
5. Introducing new eligibility criteria	Addressed as recommended.

requiring the development undertaken to increase the amount of gross floor area for eligible uses by a minimum of $500m^2$	
6. Requiring applications with over $150 million in construction value to receive council approval	Addressed as recommended.
7. Prohibiting industrial/commercial condominiums from eligibility	Ignored. The bylaws make condominium units eligible for Development grants, subject to higher standards around eligible GFA and minimum construction value.
8. Removing the requirement that the property must have been developed previously for an urban use	Addressed as recommended. The original bylaws stipulated that eligible development needed to be on sites being redeveloped, unless it was an expansion of an existing building.
9. Amending the eligibility for offices as follows: i. Add new eligibility for any office projects with a minimum gross floor area of $5,000m^2$ located within 800 metres of a subway or LRT station, except within the Financial District ii. Remove the eligibility for 'Major Office' in the Centres (see Appendices D-F) iii. Remove the eligibility for Corporate Headquarters within Downtown, except for the Financial District iv. Adding Financial Services as an eligible sector for Corporate Offices except for the Financial District	i. Addressed as recommended. ii. Addressed as recommended. It was found that even the maximum level of incentive possible would not be enough to entice Major Offices in the Centres (R. Condon, personal communication, February 19, 2019). iii. Ignored. Corporate Headquarters in the Downtown remained a targeted use. iv. Addressed as recommended.
10. Extending Film Studio eligibility throughout the City	Addressed as recommended. The 2008 City-wide bylaw targeted the development of Film Studio Complexes to three specific areas. The limitation was removed.
11. Adding Call Centres as an eligible use within the Information Services and Data Processing sector	Addressed as recommended.

Information retrieved from: City of Toronto (2012a), City of Toronto (2012b), City of Toronto (2008b)

It is interesting to note the two Hemson recommendations that were ignored in the 2012 CIP bylaws. Council decided to introduce eligibility for industrial and commercial condominium projects despite concerns raised by Hemson and seconded by ED&C staff that the administrative costs associated with tracking each condominium owner would be inefficiently high. The City likewise chose to continue offering incentives to Corporate Headquarters in the Downtown despite being advised to end eligibility of this use, presumably because such uses were no longer likely to need financial incentives. This raises concerns about the cost-effectiveness of the changes that were made to IMIT in 2012.

Council adopted By-law Nos. 1323-2012 (City-wide CIP), 1324-2012 (South of Eastern CIP) and 1325-2012 (Waterfront CIP) at its October 4, 2012 meeting.

5.3. By-law No. 1207-2018

Based on an analysis of the IMIT program's first ten years in existence, Hemson Consulting uncovered valuable insights about the program. The 31 projects that have been approved to date represent 11 million square feet of developed space and a 47,000 added or retained jobs (Hemson Consulting Ltd., 2017). The City is expected to receive an average of $29 million in net new annual tax revenue during the grant payment period and $79 million in the years following (in 2016$) (Hemson Consulting Ltd., 2017). See Appendix B for more details.

Since the program was implemented, the market for office space in Downtown Toronto has improved considerably with vacancy rates now at a historic low. 12 office projects were approved for IMIT funding, all in downtown locations. Meanwhile, there has been no program uptake for office development in Scarborough, North York and Etobicoke. This is attributable to a number of factors working in concert. In relation to neighbouring municipalities, these include: higher commercial property tax rates, fewer cost-effective surface parking opportunities and higher land costs. In relation to downtown Toronto, these include: the lack of higher order transit access and low average rents, which reduces the financial feasibility of office projects (Hemson Consulting Ltd., 2017).

On the basis of these findings, Hemson Consulting issued the recommendations outlined in Table 3. In April 2018, after tabling the report and its recommendations City staff were directed by Council to draft a new City-wide CIP By-law that would replace the previous three CIP By-laws.

Table 3 - Results of 2017 Program Review

Recommendation	Status in Bylaw 1207-2018
1. Simplify the program	Addressed as recommended. The three former CIPs are replaced with one City-wide CIP.
2. Restrict office eligibility in an expanded Financial District	Addressed as recommended. The boundaries of the Financial District are redrawn (see Appendix C) and office eligibility is restricted to a greater extent than before.
3. Maintain and simplify office eligibility outside of the core	Addressed as recommended. The previous CIP bylaws included three distinct office categories. They were replaced with a single definition for Office Building.
4. Maintain or enhance grants for other sectors and uses	Addressed as recommended. Enhanced grants for developments within Employment Areas were replaced with sector-based enhanced grants for Manufacturing, Food and Beverage Wholesaling, Creative Industries, Film Studio Complexes, and Convergence Centres.
5. Strengthen eligibility criteria for Transformative Projects	Addressed as recommended. The minimum investment requirement was increased from $250 million to $1.5 billion. The minimum gross floor area

	(GFA) requirement was increased from 75,000 square metres (over 5 years) to 200,000 (over 7 years). The minimum job creation requirement was increased from 2,500 to 3,000.
6. Enhance the Brownfield Remediation Tax Assistance (BRTA) Program	Addressed as recommended. The costs incurred for remediation within 12 months prior to application submission for the BRTA program will now be eligible for assistance.
7. Allow for IMIT grants within TIF Zones	Partially ignored. The City is phasing out IMIT Development Grants in two TIF Zones (Liberty and Queen/Carlaw).
8. Refine the administrative processes for commercial and industrial condominiums	Addressed as recommended. The new CIP requires approved condominium applicants to engage a third party facilitator to assist in administration and tracking.
9. Offer financial incentives for the replacement of office space in new mixed use developments.	Unaddressed.
10. Strengthen the program's requirements and conditions.	Addressed as recommended. The minimum construction value of IMIT-eligible projects was increased from $1 million to $3 million. Office developments will now be required to meet Tier 2 of the Toronto Green Standard, up from Tier 1.
11. Consider development charges exemption wording within the CIP By-law.	Unaddressed.
12. Consider a cap on grant approvals.	Addressed as recommended. Projects awarded an IMIT Development Grant will be subject to a cap of $30 million (exclusive of BRTA portion). This cap does not apply to Transformative Projects.
13. Improve future grant estimates	Unaddressed. This recommendation is more pertinent to program operation and therefore would be inappropriate to address in the CIP bylaw.
14. Consider a program administration fee	Addressed as recommended. A program administration fee of thirty cents per square metre, based on eligible GFA of each approved development project, will be applied.
15. Focus on ongoing marketing and promotion	Unaddressed. This recommendation is more pertinent to program operation and therefore would be inappropriate to address in the CIP bylaw.

Information retrieved from: Hemson Consulting (2017), City of Toronto (2018b)

The City made a clear move towards tightening the program's eligibility requirements. The construction value of IMIT-eligible projects was tripled to $3 million and sustainability benchmarks were raised to Tier 2 of the Toronto Green Standard. Council also elected to mitigate the costs associated with their 2012 decision to make industrial and commercial condominiums eligible for the incentives. Why this cost recovery measure was not included in the 2012 updates when Hemson had clearly flagged administrative expenses as an issue then is not clear.

In addition to these recommendations, Council considered a motion to amend the IMIT program moved by Councillor Gord Perks. The motion reads as follows:

1. City Council eliminate "office" as an Imagination, Manufacturing, Innovation and Technology (IMIT) eligible category.
2. City Council eliminate Imagination, Manufacturing, Innovation and Technology (IMIT) grants in the Smart Track Zones.
3. City Council request the General Manager, Economic Development and Culture to provide analysis of net new jobs for each Imagination, Manufacturing, Innovation and Technology (IMIT) grant in the future.
4. City Council require that every Imagination, Manufacturing, Innovation and Technology (IMIT) grant require Council approval.
5. City Council direct that the minimum eligible construction value be $3 million to be eligible for Imagination, Manufacturing, Innovation and Technology (IMIT) grants.

Parts 1, 2 and 4 lost while Parts 3 and 5 carried.

Council adopted Bylaw 1207-2018 at its July 27, 2018 meeting. The Bylaw is currently under appeal.

6. Evaluative Criteria

The Hemson Consulting report from 2017 aimed to address the following questions:

- Is the program still needed? If so, what changes if any should be made to make it more effective and cost efficient?
- What are the results and impacts of the program? Is it achieving the objectives as identified in the three Community Improvement Plans (CIPs)?
- What are the benefits and costs of the program? Do the benefits outweigh the costs?
- Are incentives needed to support the targeted development, and how extensive should they be?

To the extent that any evaluative criteria are offered, effectiveness and cost efficiency are it. In the section that follows, the IMIT program will be re-evaluated against the aforementioned criteria in addition to the following as derived from Dunn (1994) and Chianca (2008): adequacy, equity and relevance. The author – based on challenges associated with the use of property tax abatements as revealed in the literature – includes transparency as an additional criterion. Refer to Table 4 for a description of each criterion.

Table 4 - Evaluative Criteria

Criterion	Description
Effectiveness	• Whether a given alternative results in the achievement of an objective. • Often measured in terms of units of products or services or their monetary value.
Efficiency	• The amount of effort required to produce a given level of effectiveness. • Often determined by calculating the costs per unit of product or service or by calculating the volume of goods or services per unit of cost.
Adequacy	• The extent to which any given level of effectiveness satisfies the needs, values, or opportunities that gave rise to a problem.
Equity	• The distribution of effects and effort among different groups in society.

	• An equitable policy is one where effects or effort are fairly or justly distributed.
Relevance	• Are we doing the right thing? How important is the relevance or significance of the intervention regarding local and national requirements and priorities? • The value or worth of a program's objectives and the tenability of the assumptions underlying these objectives.
Transparency	• The extent to which program costs and outcomes are made publicly accessible

Information retrieved from: Chianca (2008); Dunn (1994); Kenyon et al. (2012)

7. Analysis

7.1. Effectiveness

Buried within the Hemson Consulting (2017) report is this crucial line: "while a significant amount of employment growth has been linked to the introduction of the IMIT Program, it is difficult to isolate the impact of the IMIT grants in relation to other market factors" (19). For all the good that IMIT-approved projects do for the City, it is fundamentally unclear whether IMIT grants are necessary in order to achieve those benefits.

Kenyon et al. (2012) propose a method for measuring the effectiveness of property tax incentive programs, shown in Table 5. They suggest comparing the treatment area to a control area to discern the economic impact of incentives.

Table 5 - Analyzing the True Impact of Incentives on Employment

Analyzing the True Impact of Incentives on Employment				
	Jobs Before Incentive	Jobs After Incentive (≈ 5 years later)	Difference	Explanation
Enterprise zone area with tax incentives	5,000	6,000	1,000 (6,000 – 5,000)	Simple before-and-after comparisons typically show that incentives are effective (i.e., 1,000 new jobs).
Similar area without tax incentives	5,000	5,800	800 (5,800 – 5,000)	Other economic factors could be driving job growth in some areas (i.e., 800 new jobs).
The impact of incentives on employment			200 (1,000 – 800)	Only the difference in job gains in these two areas can be attributed to incentives (i.e., 200 new jobs).

Retrieved from: Kenyon et al. (2012)

The Airport megazone offers arguably the best comparable to Downtown Toronto. Megazones are defined in Blais (2018) as “large contiguous multijurisdictional areas focused on core employment” (p. 44). Core employment in turn is defined as “jobs in tradable industries that bring revenues and income into the region and drive its growth" (Blais, 2018, p. 43). As its name suggests, the Airport megazone encompasses the area surrounding Pearson Airport, which includes parts of Mississauga and Brampton as well as a small area of north-western Etobicoke. The Airport megazone thus is not a perfect control area given that it encompasses part of Etobicoke. However, this can be controlled for as the Hemson Consulting report (2017) indicates that only one IMIT program was approved in this area of Etobicoke and created or retained no more than 1,500 jobs. In terms of scale, the Airport megazone has the second largest concentration of employment in Canada behind Downtown Toronto.

Table 6 compares core employment growth between Downtown Toronto and various megazones and Suburban Knowledge Intensive Districts (SKIDs) within the GGH.

Table 6–Core Employment by Employment Area, GGH 2006 and 2016

	2006	2016	Change 2006–2016
Downtown Toronto	345,495	412,835	67,340
MEGAZONES			
Tor-York West Megazone	119,870	119,330	-540
Airport Megazone (incl. SKID)	255,130	252,345	-2,785
Tor-York East Megazone (incl. SKID)	92,970	90,975	-1,995
MEGAZONES TOTAL (incl. SKIDS)	467,970	462,650	-5,320
Airport Megazone w/o SKID	187,405	183,095	-4,310
Tor-York East Megazone w/o SKID	54,890	52,990	-1,900
SKIDS			
Airport	67,725	69,250	1,525
Markham	38,080	37,985	-95
Meadowvale	29,385	36,155	6,770
Sheridan	5,210	5,200	-10
Waterloo	14,400	12,515	-1,885
SKIDS TOTAL	154,800	161,105	6,305
Rest of the GGH	1,437,555	1,446,110	8,555
TOTAL CORE EMPLOYMENT GGH	2,300,015	2,375,465	75,450

Retrieved from Blais (2018)

From 2006 to 2016, Downtown Toronto outperforms the rest of the GGH. Core employment growth increased by 19.5 percent at a time when all three GGH megazones experienced negative growth. Hemson Consulting (2017) purports that IMIT projects added or retained roughly 46,000 jobs in the Downtown from 2008 to 2017, equivalent to roughly two-thirds of the core job growth experienced in Downtown Toronto. While this seems to suggest that the IMIT program is responsible for most of the core employment growth in Downtown Toronto during that time period, it is unclear whether that growth can in fact be attributed to IMIT or whether it occurred for reasons independent of IMIT.

For instance by the end of the fourth quarter in 2016, Downtown Toronto's office market vacancy rate was the lowest in North America and the lowest it had ever been at 4.2 percent (CBRE Limited, 2016). It has since decreased even further to 1.9 percent in the third quarter of 2018 (Avison Young, 2018). The laws of supply and demand suggest that low vacancy rates would drive up commercial office rents, enticing new commercial office development and much of the associated employment growth.

Moreover the academic literature suggests that labour and transportation considerations vastly outweigh tax considerations in the corporate site selection process. As such, Downtown Toronto's core employment growth from 2006 to 2016 could arguably be attributed to the presence of Union Station, the high-order regional transportation hub. As Blais (2018) writes:

> This transit connectivity makes Downtown Toronto the *only* place in the GGH [Greater Golden Horseshoe] that can reliably access virtually the entire region's labour market, a critical locational factor for knowledge-intensive activities. As major roads and highways in the GGH become increasingly congested, making auto travel unpredictable and increasingly time-consuming, high-order transit provides more reliable access to jobs by workers and to workers by employers...The unparalleled access to labour is no doubt a major factor attracting knowledge-intensive firms to Downtown Toronto (p.128).

Blais also attributes this Downtown migration phenomenon to the presence of dense urban neighbourhoods that facilitate active transportation options for workers and enhanced cultural amenities like cafes, bars and restaurants. It is plausible that this combination of factors is more responsible for the observed growth in Downtown Toronto's knowledge-intensive industries than the IMIT program is.

Given that other municipalities within the region – including Brampton, Mississauga, Richmond Hill and Vaughan – have recently implemented their own tax incentive programs to encourage businesses to locate there, the effectiveness and impact of IMIT grants is likely to diminish with time.

7.2. Efficiency

The Hemson report estimates that IMIT-approved projects will result in $78.8 million in annual new tax revenue before grants. Once grants have been paid out, this amounts to an annual net gain in tax revenue of $28.8 million. Any attempt to project revenues into the future is fraught with problems. The Regent Park revitalization offers a sterling example. Toronto Community Housing Corporation (TCHC) originally projected revenues greater than $400 million from upzoning the area and planned to use the density bonuses to finance the redevelopment of social housing units that had fallen into a state of disrepair. Almost 15 years later, a $200 million revenue shortfall has put the final two phases of the redevelopment in jeopardy, with TCHC opting to re-tender those phases (Lorinc, 2018).

The Hemson (2017) report specifically noted that "the City has struggled with to [sic] develop multi-year projections for IMIT program budgeting purposes" and concluded that "the City should therefore consider requiring IMIT applicants to obtain well researched property tax forecasts from a qualified expert" (p. 56). No such requirement was enshrined in the 2018 CIP bylaw, creating concerns about whether long-term tax revenues will in fact eclipse the short-term revenues foregone as TIEGs.

Some of the program changes incorporated into the 2018 City-wide CIP bylaw do help to create efficiencies. For example, the administration fee will reduce the costs of operating the program though it is unclear to what extent if any it will discourage participation. The program cap may have a dampening effect on program participation given that large projects (as defined by the cumulative value of the TIEGs they would be paid) that do not qualify as Transformative Projects will not receive full benefit. Alternatively the $30 million grant may still be enough of an incentive in those instances to entice development, thus retaining any additional revenues that would have been foregone without negatively impacting participation.

One source of controversy around the cost efficiency of the program has been the decision to permit the issuance of IMIT development grants in areas surrounding SmartTrack stations, known as SmartTrack Zones. This proposal was first introduced in Hemson Consulting's report and then endorsed by City staff. Councillor Gord Perks submitted a motion to Council at its July 26, 2018 meeting to eliminate IMIT grants in SmartTrack Zones. This motion was voted down.

SmartTrack is to be funded in part through a modified version of tax increment financing (TIF). While the Government of Ontario passed legislation in 2006 permitting the use of TIF, no specific regulations guiding the implementation of TIF have been developed. As such no municipality in Ontario has pursued the scheme to date. The TIF scheme proposed for SmartTrack is a modified version of that found in the enabling legislation.

TIF presumes that the development of SmartTrack infrastructure will create greater demand for properties in SmartTrack Zones, increasing land values in the Zones. The municipal tax revenue increment is then used to fund a portion of the debt that was initially incurred to finance the SmartTrack infrastructure. However, Councillor

Perks notes that to provide IMIT grants in SmartTrack Zones would mean forgoing municipal property tax revenues that are already earmarked for financing SmartTrack debt. City staff have responded by saying that while SmartTrack would likely catalyze new development, the pace of that development and thus the pace at which the City recovers its initial investment is uncertain. IMIT grants ensure new development occurs faster and stronger than would otherwise be the case, allowing the City to recapture its initial investment on an expedited basis (Toronto City Council, 2018).

Using tools in simultaneity that work fundamentally counter to one another is an inefficient and perhaps ineffective means of achieving an objective. Furthermore the objective of the IMIT program is to incentivize development that would not have occurred but for the incentive i.e. *but for* the IMIT grant, the proposed development would not have occurred. This is the foundational test upon which all IMIT grant funding rests. City Manager Giuliana Carbone clearly stated her belief that development would occur in SmartTrack Zones <u>without</u> the IMIT grants, just that it might take longer (Toronto City Council, 2018). Therefore by City staff's own admission, projects in SmartTrack Zones do not meet the but-for test.

7.3. Adequacy

Despite the litany of Official Plan policies aimed at directing population and employment growth to the Centres, the IMIT program has done an inadequate job of encouraging commercial office development in these focus areas. This is demonstrated by the fact that no new office development has been proposed in the Centres since the program's inception. In fact, since 1992 only one new office building has been constructed in the Centres (City of Toronto, 2008b).

According to City staff, when the program was first proposed the City studied the level of incentive that would be needed to entice said growth. It was found that even a full property tax abatement over 10 years would be insufficient (R. Condon, personal communication, February 12, 2018). The City through its 2008 city-wide CIP bylaw did offer to provide grants for Major Office Development in the Centres. The grants were removed in the 2012 city-wide CIP bylaw in order to simplify the program (R. Condon, personal communication, February 12, 2018). However no additional supports or incentives were created to aid the development of the Centres.

7.4. Equity

In most US states, census tract areas must meet a set of criteria that prove they are economically depressed (unemployment, poverty and low income being the predominant metrics of this) before they can qualify as "enterprise zones" under state law and provide tax incentives. As a result, enterprise zones tend to be quite small (Kenyon et al. 2012).

The CIP provisions in the *Planning Act* provide no such requirements, instead giving municipalities full authority to designate CIPAs as they see fit. This arrangement has allowed the City of Toronto to designate the entire municipality (excluding the Expanded Financial District) as a CIPA, most recently through By-law No. 2107-2018. The effect of this blanket approach to economic development is that economically disadvantaged areas are treated the same as their advantaged counterparts. It is therefore of little surprise that development has accrued in the more economically advantaged areas, for instance the Financial District.

Of particular note is the fact that the IMIT program has not led to the development of any office buildings in the Centres while providing $266 million in TIEGs to support office projects in and around the Downtown. A 2012 recommendation by the General Manager, ED&C to remove eligibility for Corporate Headquarters in the Downtown was ignored by Council. Rather than invert the program structure and target depressed communities, the solution thus far has been to progressively expand the IMIT-ineligible area centred around the Financial District. It is reasonable to assume that new targeted sector development will simply "hug the edges" of the IMIT-ineligible area, leaving communities at the city's fringes no better off than they were before.

The program is also unfair in that it benefits new firms moving into the city while offering no advantage to existing firms that have contributed to the tax base potentially for years and decades. Other tax initiatives that affect all firms alike regardless of tenure, such as the reduction in ratio of commercial and industrial property tax rates to residential property tax rates, are more equitable.

7.5. Relevance

Each of the three City-wide CIP bylaws that have been approved by Council since 2008 have declared the bylaws' primary objectives to be to encourage brownfields remediation and the development of targeted employment uses within the City. Meeting Toronto's Growth Plan employment targets is an expected outcome of the IMIT program but not a primary objective, a position confirmed in interviews with City staff (R. Condon, personal communication, February 12, 2019).

Groups such as the Toronto and York Region Labour Council have stated that their support for the IMIT program was contingent on "the creation of good, stable jobs that pay living wages and allow Torontonians to prosper" being the "foundational benchmark" of the initiative (McMurray, 2018, p. 1). They claim that

> very little is known about the jobs that are established in those businesses that are owner or tenant users of the newly-developed spaces...jobs appear to be an afterthought, with much attention focused on the total value of construction, square footage, tax revenues, etc." (McMurray, 2018, p. 2).

Users of IMIT-approved developments are required to work with Toronto Employment and Social Services (TESS) to develop a Local Employment Plan that provides employment opportunities to City of Toronto residents (City of Toronto, 2016). The strictness and long-term enforceability of these plans is unclear however. Crucially there is no minimum jobs requirement developers must meet in order to receive IMIT grants. Although there is an annual reporting requirement enforced on grant holders, it does not include an obligation to report on the number and type of jobs created or retained (R. Condon, personal communication, February 12, 2019). This may change soon as Council approved a motion in 2018 that would require the General Manager, ED&C to report on the number of net new jobs created for each future IMIT grant.

The objectives underpinning the IMIT program are fundamentally misaligned with the priorities and needs of City of Toronto residents: the creation of well-paying, secure jobs in growing sectors of the global economy. By focusing on metrics such as square footage and construction value of targeted uses, the IMIT program neglects to ensure that employment growth is commensurate with the expansion of said uses. Some targeted uses are even of questionable merit. The sustainability and stability of Manufacturing employment is unproven. The knowledge-intensity and wage level of Tourism Attraction and Call Centre employment is also unverified.

7.6. Transparency

There is no legal basis for the but-for test. With the exception of Transformative Projects and Tourism Attractions, there is no requirement contained in any of the CIP bylaws that applicants must pass a but-for test in order qualify for IMIT funding (Andres, 2018). Yet the test is foundational to the administering of IMIT grants across all targeted sectors. Furthermore it is not clear how the but-for test is applied i.e. what pro forma-based assumptions are made in determining whether an applicant would dissolve a project if not for the incentive. Applicants are faced with the reality that they could meet all of the minimum eligibility requirements for funding but be rejected on the basis of a non-statutory test that, the application of which may be completely arbitrary for all anyone knows. The tax-paying public is faced with the reality that public revenues are being diverted to private property owners based on a test which they cannot scrutinize. There is a genuine and problematic lack of transparency inherent in the but-for test.

For the largest applications which require Council approval, City staff do solicit an independent third party opinion (R. Condon, personal communication, February 12, 2018). However the fundamental lack of transparency is still present given that the assumptions upon which the third party bases its analysis are once again not readily and publicly available for scrutiny.

What is clear however is that for projects that exceed $150 million in construction value, ultimate approval authority lies with Council. During the 2018 review of 8 IMIT applications that required Council approval, some Councillors argued that City staff and the third party reviewer had unfairly judged these applications against criteria that were not yet in place when the applications were submitted. This argument does not hold water. The 2012 CIP by-laws – in addition to the 2018 CIP by-law still under review – require Council approval for all projects where construction value exceeds $150 million. Furthermore City staff have indicated that in pre-submission meetings with applicants for projects where Council approval would be required, applicants are never told they will receive IMIT funding for simply meeting minimum eligibility requirements (Toronto City Council, 2018).

8. Conclusions

Due to the nature of the IMIT program, it is difficult to discern its overall effectiveness and efficiency level. Downtown Toronto in terms of core employment growth has performed quite well since 2008 relative to the rest of the region. However, the literature as well as market conditions suggest that the main credit for this cannot be assigned to the IMIT program.

Far clearer are the challenges associated with adequacy, equity, relevance and transparency. The inability of the program to reach the Centres is significantly detrimental from an adequacy and equity perspective. The lack of focus on employment threatens the relevance of IMIT. Finally the process through which grants are administered is underpinned by a test with no legislative basis and no clear criteria.

9. Recommendations

1. **Eliminate the IMIT program**.

There is no feasible way of determining whether the firms that apply for IMIT grants would choose not locate within the City but for the incentive. There is nothing preventing these firms from escalating expenses or deflating revenues in order demonstrate need where there is none. Every firm uses a different rate of return to decide whether a project is worth constructing and the very premise of the but-for test requires City staff to determine for itself what the "going" rate of return for the industry is. Expecting that all firms conform to the industry standard is unrealistic and ineffective. The City is not privy to the expertise required to make the correct determinations and certainly does not have the moral authority to selectively offer grants on the basis of the blunt determinations it does make.

The entire foundation upon which the program rests is one of confidentiality, and thus one lacking in transparency for the tax-paying public. The City cannot make public the assumptions that underpin its but-for test, for applicants would tailor their pro formas to demonstrate need as per those assumptions. However, applicants are expected to trust the City's assumptions are reasonable and are applied fairly across firms and projects. This lack of transparency is inherent to the functioning of the program. To remove the test would enable all firms to profit from the incentive regardless of need, which would create further strains on municipal revenues while not creating any demonstrable benefit to the City. To publicize the assumptions underpinning the but-for test would render the test useless and create the same result. In the name of transparency and fairness, the only tenable solution is to abolish the program.

The literature suggests that reinvesting IMIT grants into human and infrastructure capital would have a greater impact on the locational decision-making of firms. Furthermore the need for these investments is relatively transparent (though admittedly the prioritization of needs is always inherently political) and certainly not reliant upon a secretive test riddled with assumptions that cannot be made public.

Given that there is currently little political appetite for the elimination of the IMIT program, the following alternative recommendations are offered.

2. **Make well-paid, stable employment the foundation of the program.**

   There is far too much emphasis placed on increasing square footage of eligible uses and sectors and too little attention paid to employment considerations. The fact that it took a decade for Council to agree that net new jobs ought to be forecasted for IMIT projects in order to more holistically understand the City's return on investment is evidence of this.

3. **Scale down the geographic scope of the IMIT program to the Centres, in addition to economically depressed areas of the City such as Neighbourhood Improvement Areas.**

   In the midst of a lucrative commercial office market in the Downtown, a City-wide approach is not an effective or efficient use of tax revenues. Scarce municipal resources must be more strategically targeted towards areas that lack knowledge-intensive employment opportunities. Should this strategy fail to attract the desired level of growth, then the City should redouble its efforts to invest in Toronto's human and infrastructure capital.

4. **Adopt a more transparent model for assessing applications and awarding funding.** Similar to the City, the Region of Niagara offers a Tax Increment Based Grant (TIBG). Unlike the IMIT program however where funding is awarded based on an extra-legal but-for test and all grants are equivalent to 60 percent of the tax increment over ten years, the TIBG is awarded on clear criteria related to projects' economic and environmental design performance and the amount awarded is geared to said performance (Niagara Region, 2015). The IMIT program could potentially benefit from a points-based system for administering grants.
5. **Eliminate IMIT grants in SmartTrack Zones.**

Using both TIF and TIEGs in conjunction is nonsensical given that these tools operate at odds with one another. The tax increments in SmartTrack Zones should either be used to pay off debt obligations associated with SmartTrack infrastructure or paid back to property owners to entice development that otherwise would not happen. The former is the more sensible option. Transit improvements should catalyze development and if there is serious concern that it will not, then TIF has not delivered on its reputation as a viable transit financing tool and should not be utilized by the City to fund SmartTrack.

6. **Eliminate Call Centres, Tourism Attractions and Manufacturing from the list of eligible sectors and uses.**

The former two sectors are not widely recognized as creating well-paying, knowledge-intensive jobs. To the extent that the City should be involved in subsidizing private firms to create employment, this is not the type of employment the City should be using scarce municipal resources to subsidize.

Blais (2018) argues that call centres and manufacturing are highly vulnerable to automation, with the latter additionally susceptible to trade disruption. Between 2006 and 2016, employment in manufacturing within the GGH declined by 25 percent (Blais, 2018). This charts a broader trend experienced in OECD countries (Statistics Canada, 2018). The City should not be subsidizing firms in declining sectors of the regional and developed economies to locate in Toronto.

10. Final Remarks

During the Amazon bid process, Toronto set a standard for itself that came to be widely admired. The City on principle refused to offer firm-specific tax incentives, instead relying on other competitive advantages to make its case. Unfortunately this has been the exception rather than the rule. For the last ten years, Toronto has institutionalized the practice of offering tax abatements and tax increment equivalent grants to firms that develop eligible workspace within the City. These abatements and grants will in the coming years total hundreds of millions of dollars in foregone tax revenues that the City could be using to address municipal priorities, such as transit construction and social housing repair. In the context of an increasingly economically and geographically segregated city, IMIT grants have reinforced growth in the core while defunding critical infrastructure and human capital upgrades in areas that need them to be competitive. The time has come for the City to reinvest in itself by eliminating the IMIT program.

Appendices

Appendix A - CIP Bylaw Comparison

	2008 CIP bylaws	2012 CIP bylaws	2018 CIP bylaw
The Centres	Development Grants for Major Office Development	None	None
Waterfront and South of Eastern	Separate bylaws from City-wide	Separate bylaws from City-wide	Amalgamated with City-wide
Employment Districts (EDs)	Explicit goal of investing in EDs	Explicit goal of investing in EDs	Investment in EDs not explicitly mentioned in CIP objectives
Targeted Sectors	• Biomedical • Computer Systems Design and Services • Convergence Centres • Corporate Headquarters, in Downtownor on Sites in Subway Corridors • Creative Industries, excluding Film Studio Complexes • Food and Beverage Wholesaling • Incubators • Information Services and Data Processing • Manufacturing, provided the manufacturing operation occupies at least 40% of the GFA • Scientific Research and Development	• Biomedical • Call Centres • Computer Systems Design and Services • Convergence Centres • Corporate Headquarters, in Downtown • Creative Industries • Film Studio Complexes • Food and Beverage Wholesaling • Incubators • Information Services and Data Processing • Manufacturing, provided the manufacturing operation occupies at least 35% of the GFA in a single use building or facility • Scientific Research and Development • Software Development	<u>General Grants</u> • Call Centres • Computer Systems Design and Services • Information Services and Data Processing • Scientific Research and Development • Software Development • Tourism Attractions • Transformative Projects, subject to approval by City Council <u>Enhanced Grants</u> See cell below

	• Software Development • Tourism Attractions • Transformative Projects, subject to approval by City Council	• Tourism Attractions • Transformative Projects, subject to approval by City Council	
Enhanced Grants	None	Offered for developments in EDs and other designated Employment Areas.	Offered for developments containing Biomedical, Manufacturing, Food and Beverage Wholesaling, Creative Industries, Film Studio Complexes, Convergence Centres and Incubators.
Office Buildings	Grants available only if office building user is in one of the following sectors: • Biomedical • Creative Industries • Computer Systems Design and Services • Food and Beverage Wholesaling • Information Services and Data Processing • Manufacturing • Scientific Research and Development • Software Development	Grants available if office building user is not located in the Financial District and is in one of the following sectors: • Biomedical • Creative Industries • Computer Systems Design and Services • Food and Beverage Wholesaling • Information Services and Data Processing • Manufacturing • Scientific Research and Development	Grants available if office building user is not located in the Financial District and has a min. GFA of 5,000 m2 or in for a mixed-use building a min. contiguous GFA of 5,000 m2 Eligible office space provided through an office replacement policy is not subject to a minimum size requirement.

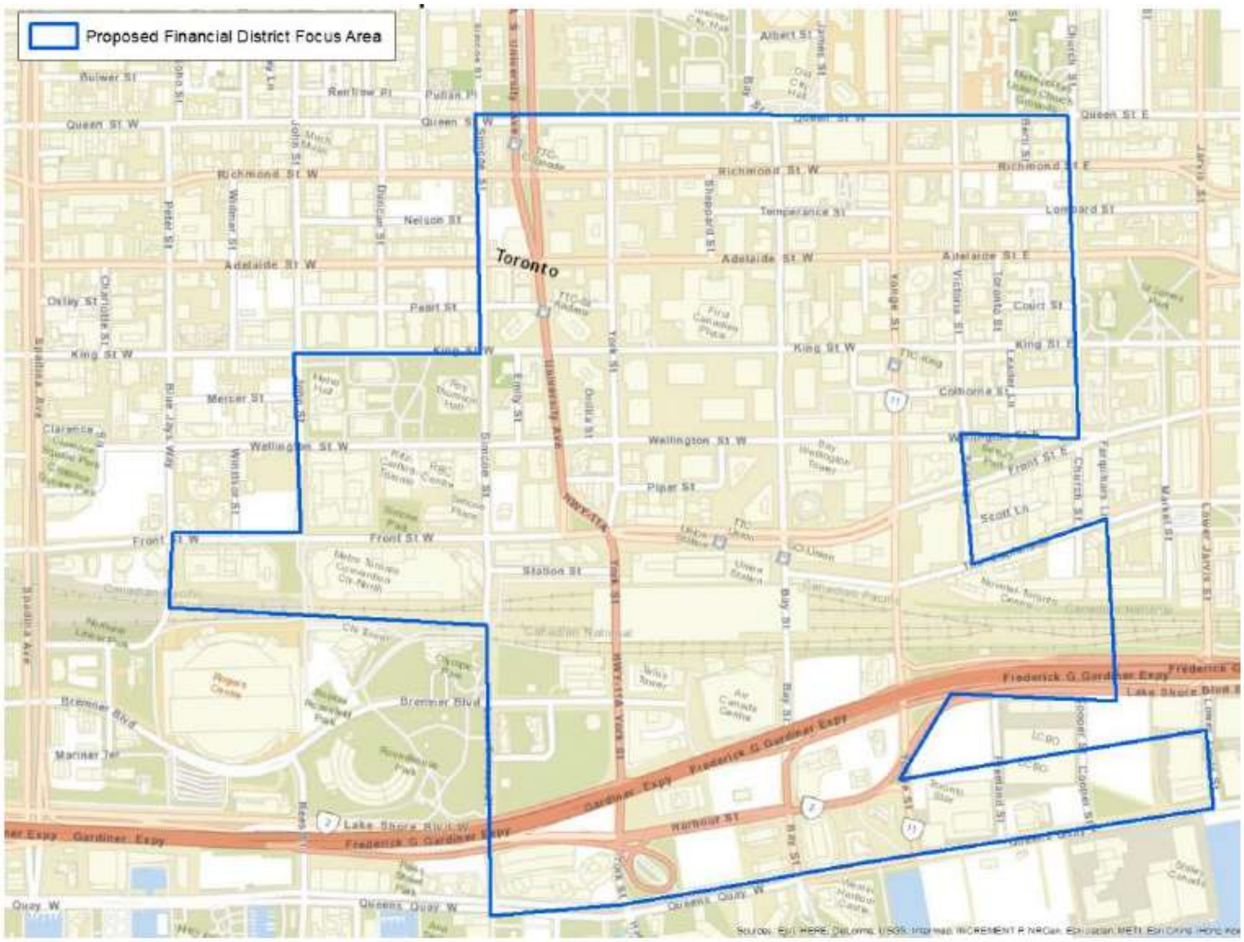
		• Software Development Grants also available for any office building with a min. GFA of 5,000 m2 located on sites in Transit Corridors (excl. Financial District).	
Condominiums	No policy	Each condo unit to be treated as stand-alone development and must meet all eligibility requirements independent of other condominium units, with the following additional requirements: • the condo unit must comprise at least 5,000 m2 of eligible GFA; and • the condo unit must have a construction value of at least $5,000,000.	A third party facilitator must be engaged by the applicant to assist in administration and tracking of Development Grants. All costs associated with this third party facilitator are the sole responsibility of the applicant.

Appendix B - IMIT Key Program Indicators

IMIT Applications Approved To Date (Signed Financial Incentive Agreements)							
Sector/Use	Projects	Estimated Eligible GFA (sq.ft.)	Estimated Eligible Construction Investment(1)	Estimated Employment (Retained + New)	Estimated Average Annual Grant Total(2,3)	Estimated Annual New Tax Revenue Before Grants(4)	Estimated Annual New Tax Revenue Net of Grants
Office	12	$5,646,000	$1,973,160,000	28,800	$24,063,000	$39,393,000	$15,330,000
Manufacturing / Food & Beverage Wholesaling	8	1,125,000	$281,144,000	1,500	$1,854,000	$2,662,000	$808,000
Information Services & Data Processing	1	220,000	$80,124,000	100	$910,000	$1,250,000	$340,000
Incubator / Convergence	5	960,000	$239,904,000	3,400	$3,478,000	$6,103,000	$2,625,000
Creative Industry / Film Studio	3	355,000	$118,477,000	800	$543,000	$932,000	$389,000
Tourism	1	101,000	$107,000,000	300	$684,000	$922,000	$238,000
Transformative Project	1	2,700,000	$985,500,000	12,500	$18,450,000	$27,537,000	$9,087,000
Total	**31**	**11,107,000**	**$3,785,309,000**	**47,400**	**$49,982,000**	**$78,799,000**	**$28,817,000**

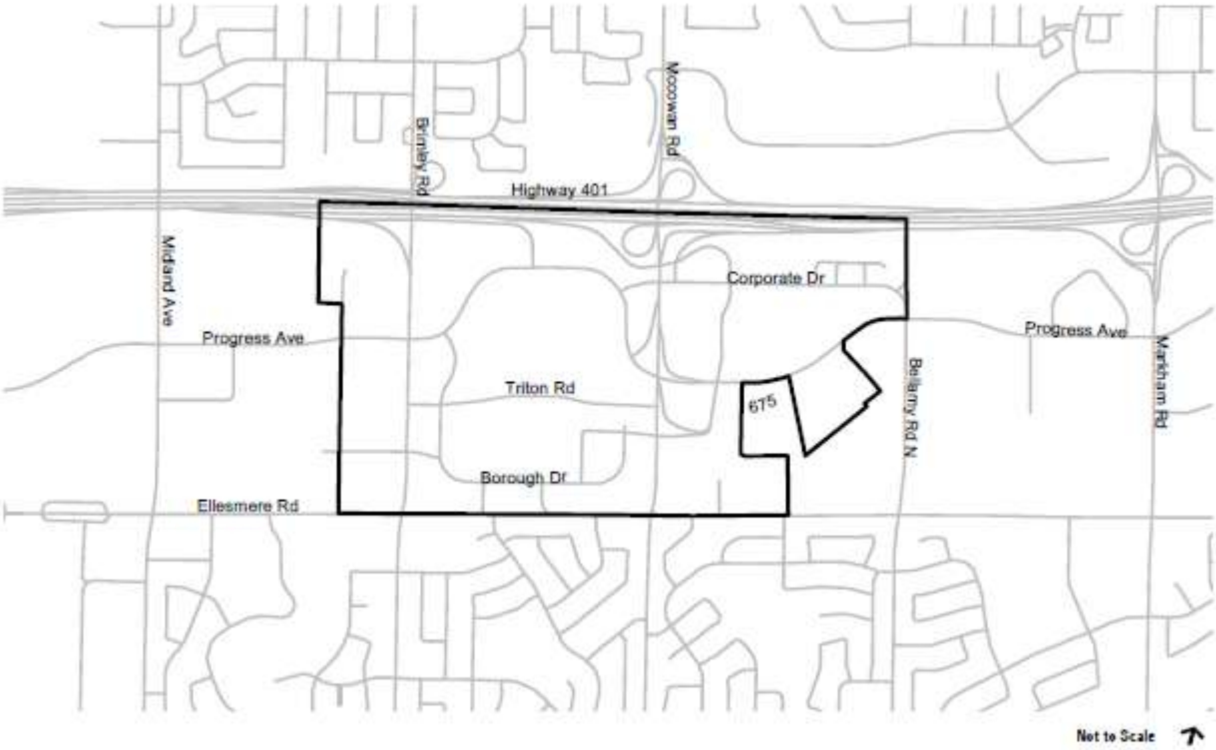
Retrieved from Hemson Consulting Ltd. (2017, p.21)

Appendix C - Proposed Financial District Focus Area



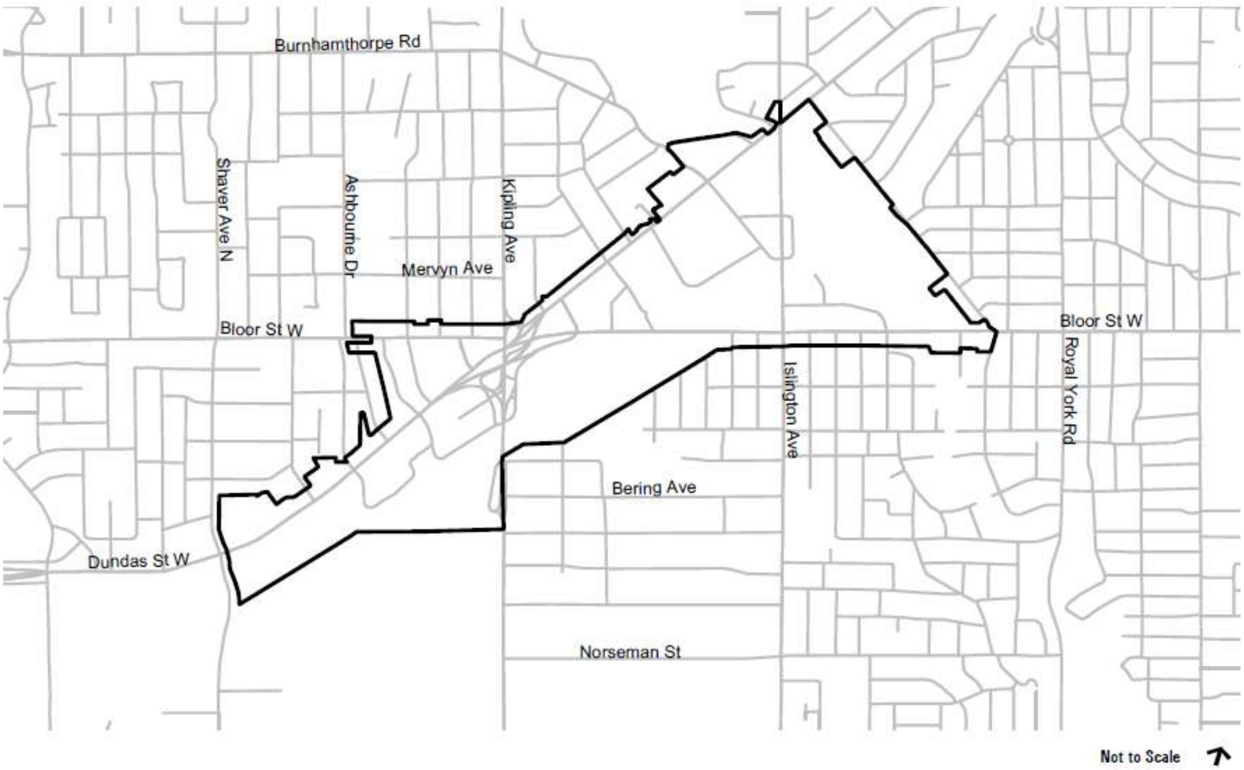
Retrieved from Hemson Consulting Ltd. (2017, p.50)

Appendix D - Scarborough Centre



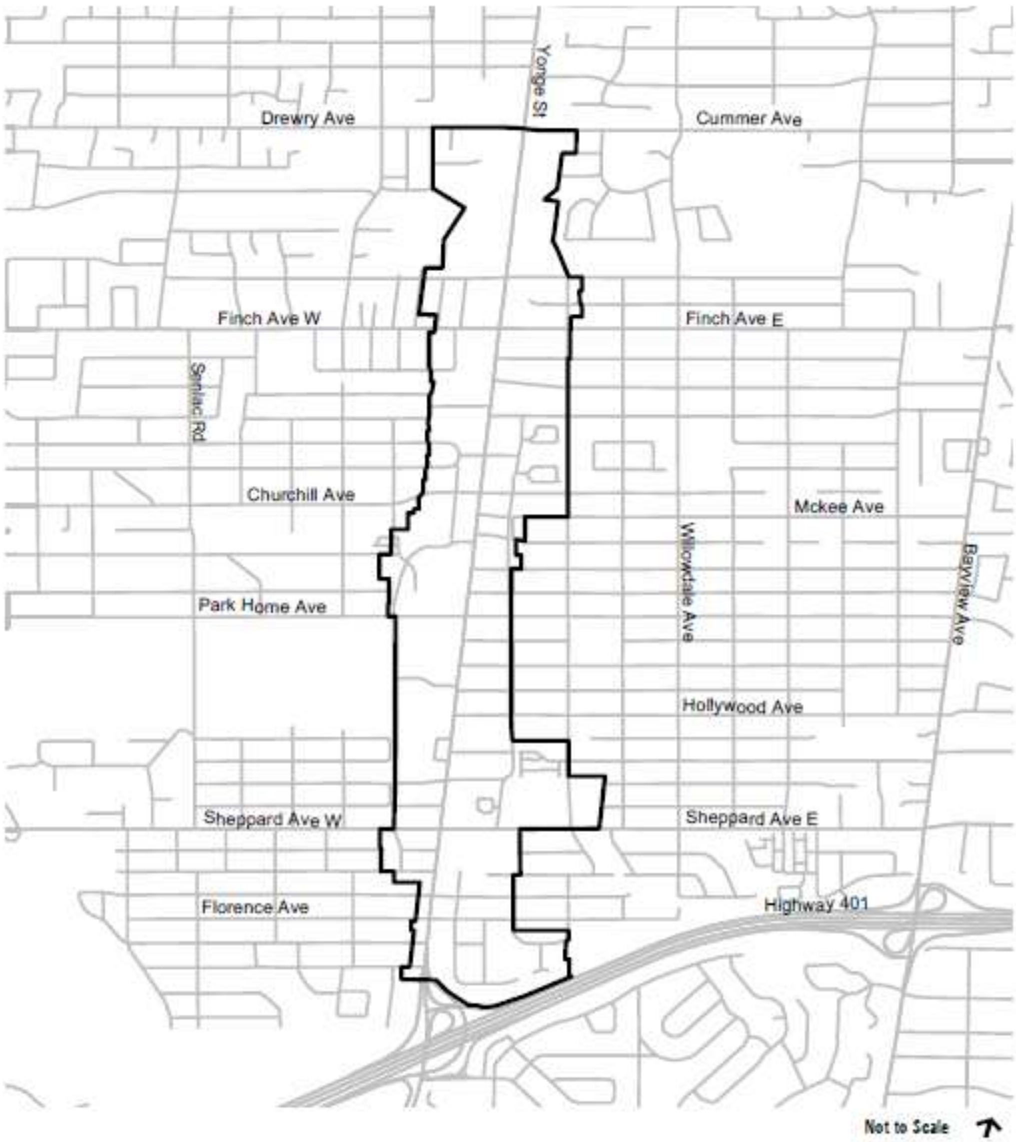
Retrieved from City of Toronto (2018b)

Appendix E - Etobicoke Centre



Retrieved from City of Toronto (2018b)

Appendix F - North York Centre



Retrieved from City of Toronto (2018b)

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