



ONTARIO RESTAURANT HOTEL & MOTEL ASSOCIATION

**Submission to the Standing Committee on  
Finance and Economic Affairs**

**2004 Pre-Budget Consultations**

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## **Introduction**

### ***What is the Ontario Restaurant Hotel & Motel Association?***

The Ontario Restaurant Hotel & Motel Association (ORHMA) is Canada's largest provincial non-profit industry association that represents the interests of Ontario's foodservice and accommodation sectors. The ORHMA is dedicated to fostering a positive business environment for Ontario's hospitality industry, while providing value-added services to its members.

These benefits include cost-saving initiatives, group-purchasing programs and educational services. The ORHMA's Government Relations Department represents the industry's interests to the Government of Ontario and City Halls across the province on issues such as taxation, business regulation, beverage alcohol, labour issues, public health, municipal bylaws and tourism.

### ***Profile of Ontario's Hospitality Industry:***

Ontario's hospitality industry is one of the most dynamic and competitive sectors of the provincial economy, generating \$18.32 billion in annual sales and 4.3% of provincial GDP. With more than 22,200 foodservice establishments and nearly 3,000 accommodation properties across the province, the hospitality industry directly employs over 411,000 Ontarians. This represents 7% of total employment. The contribution made by this economic sector is felt in all regions of the province and affects the livelihood of many of Ontario's residents.

### ***Foodservice Industry Highlights:***

- \$16 billion in sales
- 22,200 units (63.1% owned and operated by small, independent operators)
- 5.9% of total provincial employment (354,000 direct jobs)
- 17.4% of youth employment is in the foodservice sector (154,700 direct jobs)

- Foodservice industry employment accounts for approximately 46% of all persons employed in the entry-level segment of the Ontario economy. These Ontarians rely primarily on the foodservice industry for employment.
- Average profit margins within the industry are a mere 5% after tax.
- The average full-service restaurant contributes \$173,232 in taxes annually to all three levels of government.
- 17% of an operator's tax burden comes from property taxes.

### ***Accommodation Industry Highlights:<sup>1</sup>***

- \$2.3 billion in room sales
- 813 establishments with 30 rooms or more, 2100 with less than 30 rooms
- Direct employment is approximately 52,000.
- Almost \$1.4 billion in wages and benefits are paid by the accommodation sector to Ontario workers annually.
- The accommodation industry contributes over \$1.3 billion in taxes annually to all levels of government.

### ***State of the Industry:***

This past year has been the most challenging that Ontario's hospitality industry has ever experienced. The immediate economic impact of the SARS outbreak was previously unimaginable. Having struggled through the effects of lower corporate spending in recent years, the tragic attacks on America on September 11th, the War on Terror, strained Canada-US political relations, the War in Iraq, SARS I, SARS II, mad cow, the strong Canadian dollar and this past summer's province-wide blackout, Ontario's hospitality industry has suffered enormous setbacks.

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<sup>1</sup> (Please note that these statistics exclude accommodation properties with less than 30 rooms, unless explicitly stated. In Ontario, accommodation properties with less than 30 rooms represent over 50% of the establishments.)

In the first nine months of 2003, Ontario saw a continued decline in the number of international border crossings of 13.8%.<sup>2</sup> This continues a pattern established in 2002 when international border crossings were 11.1% lower than 2001 levels.<sup>3</sup> While projections estimate that total international border crossings for 2003 will be 5.2% lower than the previous year, in the fourth quarter alone, the hotel sector is expected to lose a further \$14.3 million in room revenue due to cancelled business.<sup>4</sup>

International travelers are vital to the Ontario hospitality industry and this continued downward trend must be corrected. **The cumulative impact of these external factors has caused Ontario's hospitality industry to lose over \$1 billion in tourism spending during 2003.**<sup>5</sup>

### ***Government Policy:***

Government has a significant role to play in Ontario's hospitality industry's recovery. The Association and its members understand that the Government faces a number of significant challenges, not the least of which is the Province's reported \$5.6 billion deficit. However, considering that the Ontario economy is 26 times larger than Ontario's hospitality industry and yet the provincial deficit is only five and a half times larger than the tourism spending losses experienced by Ontario's hospitality sector, it would seem that that Ontario's hospitality operators have financial problems of their own without having to shoulder a disproportionate share of the Province's fiscal troubles.

But that is exactly what has occurred within the first 100 days of the Government's term.

For illustrative purposes, the following outlines the impact of Government decisions on an average restaurant.

- An increase to the capped hydro rate: \$4,250
- An increase to the minimum wage: \$3744
- A repeal of the scheduled corporate and small business tax cuts: \$9040

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<sup>2</sup> Ontario Tourism Facts & Figures, Ministry of Tourism and Recreation, Winter 2003-04

<sup>3</sup> Ontario Tourism Facts & Figures, Ministry of Tourism and Recreation, Fall 2002

<sup>4</sup> Tourism Research Indicators, 2003 in Quarters, Ministry of Tourism and Recreation, Nov. 2003

<sup>5</sup> KPMG, Tourism Expenditure Monitor, Winter 2003

- Introduction of the new packaging recycling tax: \$1000

The estimated increases to the cost of doing business, as a result of the decisions made by the Government during their first 100 days, of the new government, for the average restaurant has increased by \$18,034.

It is vital that the Government understands the cumulative impact that these decisions will have for an ailing hospitality industry and it is within this context that our members across the province are extremely concerned with other proposals that the Government has considered publicly.

- Imposing the Employer Health Tax on Small Business
- Adding an additional percentage to the Retail Sales Tax
- Eliminating the tax deductibility on Business meals
- Eliminating the \$4 RST exemption threshold on meals
- Increasing beverage alcohol floor prices, fees and taxes
- Lifting of the commercial property tax caps
- Introduction of a province-wide smoking ban
- Eliminating second-year SARS recovery investment and the elimination of the OTMP

The Government must understand that the impact of any of these proposals would cost Ontario's hospitality employers tens of millions of additional dollars in reduced sales, increased expenses, or both. This is the wrong time to continue to increase the burden on Ontario's hospitality industry.

A thriving hospitality industry translates directly to employment and tax revenue generation for the province. The Government has a significant opportunity to bolster the strength of the hospitality industry, while maintaining a fiscally responsible approach to provincial finances.

The Government must ensure that confidence in Ontario's fiscal management remains high by outlining a responsible timeline in which to balance the budget and make a serious commitment to this schedule. The Government should not, however, simply make a politically expedient decision to rush a balanced-budget in taxation frenzy. While increased tax revenue generated by rate hikes can bolster the provincial coffers in the short-term, higher rates could endanger future economic growth.

The Government must also make strategic investments that generate significant economic activity in an effort to grow provincial tax-revenue. Strategic investment in tourism marketing is one area that holds tremendous returns.

**Return on investment figures show that for every dollar invested in hospitality and tourism marketing, \$20 of economic activity is generated.<sup>6</sup>**

More must be done to increase travel to Ontario, bringing significant amounts of new money into the provincial economy, fostering capital investment, creating jobs and boosting provincial tax revenues.

Finally, the Government must ensure that the cost of doing business in Ontario remains competitive with other jurisdictions. While tax rates must be competitive, to attract investment and foster growth, the Government must also appreciate and fully consider the impact of the non-tax costs of doing business including municipal user fees, Stewardship Ontario fees, liability insurance rates, WSIB premiums, beverage alcohol prices, hydro costs, administrative costs created by red-tape and labour costs. The Government must take action to ensure that these general business-operating expenses are minimized and do not jeopardize competitiveness and employment.

Recognizing the unique challenges that the Government faces, the Ontario Restaurant Hotel & Motel Association recommends a number of policies that will allow the Government to foster the industry's recovery and leverage Ontario's hospitality industry as a tax revenue and employment generator for the provincial economy.

## **Issues**

### **Investment in Tourism Marketing**

Despite the negative, and often exaggerated, media coverage of SARS, Ontario remains a safe and exciting world-class destination with a tremendous diversity of activities and attractions. Both geography and culture make Ontario a very competitive destination. However, in relation to tourism marketing, it has been less than competitive. For years, Ontario has run a 'promotional deficit' relative to other jurisdictions.

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<sup>6</sup> Metro Toronto Convention Centre, Winter 2003

Until recently, the province invested only a very modest \$30 million per year in tourism marketing. By comparison, Montreal invests \$22 million annually, Vancouver \$12 million, Chicago over \$80 million and Boston nearly \$30 million. It is clear that a province the size of Ontario needs to invest more in tourism marketing to remain a competitive and visible choice for prospective visitors. Continuing down the road of a 'promotional deficit' will lead to only long-term losses in economic activity, employment and government revenue.

**Over the four-year period leading up to 2003, Toronto alone lost 8.2 million visitors to competing destinations. This loss represents \$2.3 billion dollars in lost revenue and \$411 million in lost tax dollars.<sup>7</sup>**

Neither Ontario's hospitality industry nor the Province as a whole, have not been well served by its long-standing promotional deficit. In response to the SARS outbreak, the provincial government made a significant \$128 dollar, two-year investment in SARS recovery funding with the recognition that the recovery process would require a long-term commitment.

The Association was pleased to learn that the current Government understands the importance of SARS recovery investment and has approved funds for the first six months of the second-year funding component. While this is a promising start, it is vital that all remaining original SARS investment money is allocated. The Government must also commit to long-term, stable funding that will allow Ontario to remain competitive in the global travel destination market.

The ORHMA was also encouraged that the Government's funding commitment to the Ontario Tourism Marketing Partnership Corporation (OTMP) was extended for a six-month period. The Association understands that the Government is currently reviewing the current structure of OTMP and is giving consideration to a proposal that would see OTMP moved into the Ministry of Tourism & Recreation. However, the Association believes that OTMP, in its current form, is fulfilling its mandate in bringing public and private sector investment together in the promotion of Ontario. There is significant concern, that if the OTMP was absorbed by the Ministry of Tourism, private sector contributions would be more difficult to solicit.

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<sup>7</sup> Greater Toronto Hotel Association, Fall 2002

## Recommendation:

The ORHMA recommends that, to regain its competitive position in relation to other jurisdictions and to continue its recovery from the economic impact of SARS, the Ontario Government make a strategic, multi-year tourism investment commitment beginning with the allocation of the remaining second-year, SARS recovery investment.

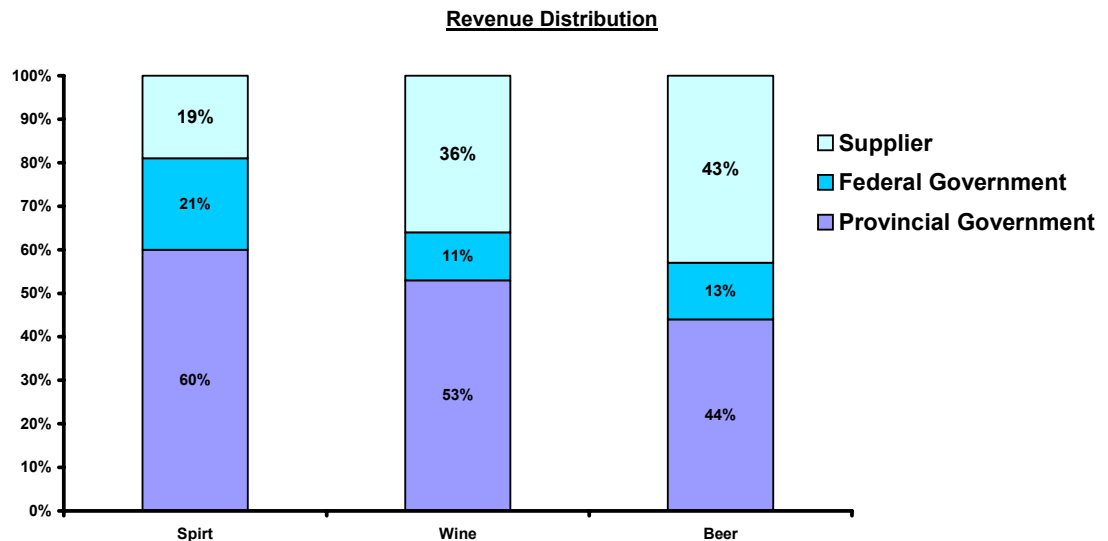
The Association also recommends that the Government continue to support and fully-fund the efforts of the Ontario Tourism Marketing Partnership Corporation and that the OTMP remains as a public-private partnership at arms-length from Ministry of Tourism and Recreation.

## Beverage Alcohol Reform

The alcohol pricing structure in Ontario is very complex. Unlike other consumer products, prices not only reflect the manufacturers' cost, the wholesale and retail markups and the federal and provincial taxes, but there is also an intricate system of additional fees and levies that drive-up the cost of serving wine, beer and spirits as a licensee.

The following chart represents the revenue distribution on products sold in Ontario. (Graph A)

Graph A<sup>8</sup>



<sup>8</sup> LCBO Annual Report 2000-2001

The large percentage of provincial revenue illustrated in the above chart is not simply derived from the 10% provincial alcohol sales tax. Since the provincial government controls the wholesale and retail distribution network, retail markups and embedded fees boost provincial revenue.

However, some of this provincial revenue is generated through double taxation. More than any other tax, the gallonage fee currently applied to beer, spirits and wine purchased for resale by licensed establishments is wholly unjustified, as it supports taxation on top of taxation.

Currently, licensees in Ontario pay two separate and distinct licensing fees. One licensing fee is a fixed annual licence fee and the other is a variable volume or price-based fee (gallonage fee) applied to licensee purchases of beer, wine and spirits.

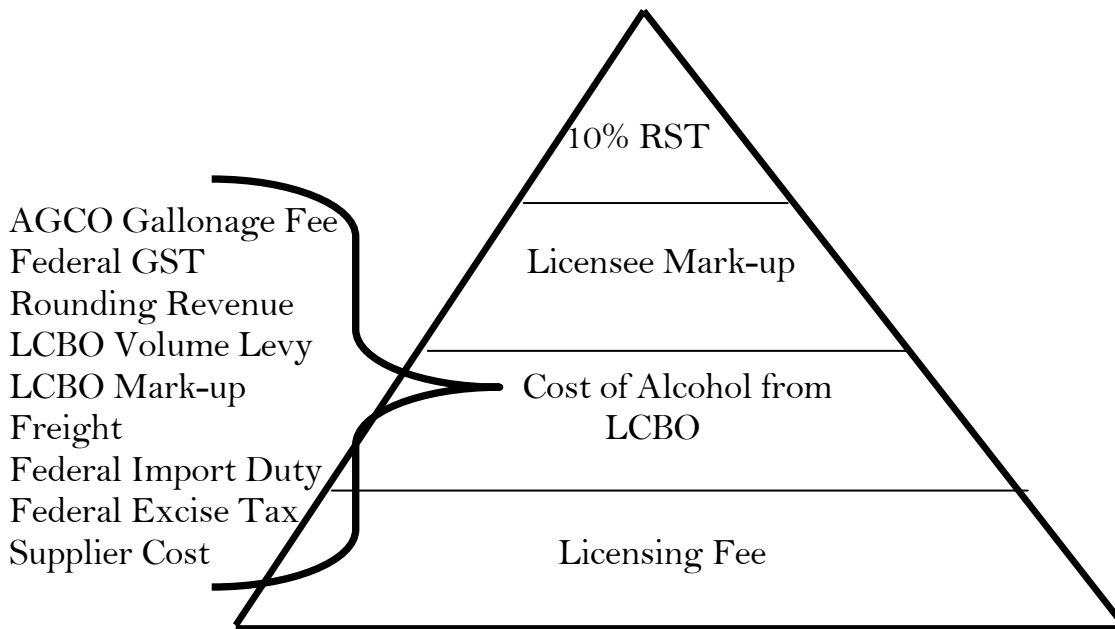
According to the *Liquor Licence Act*, applicants for a liquor licence are required to pay application fees of \$685 or \$815 depending on whether public notice is requested, pay for the cost of the public notice, pay a fee of \$240 upon the issuance of a liquor licence, and pay a renewal fee of \$300.

In addition to these licensing fees, licensees are further required to pay an additional fee, known as the gallonage fee, which is:

- a) \$2.64 per hectolitre of beer purchased for sale or consumption under the licence; and,
- b) an amount equal to 12% of the purchase price of wine and spirits, including the price of containers, purchased for sale or consumption under the licence.

This results in two fees for every licensed establishment. After being charged these two fees, one on the purchase of alcohol, licensees are required to charge an additional tax (10% RST) upon the sale of beverage alcohol to their customers.

**Provincial Alcohol Tax Structure:  
A TAX, ON A TAX, ON A TAX**



The complex licensing, pricing and taxation structure for alcohol requires a full governmental review. Given the Government's recent consideration regarding the privatisation of the LCBO, the Association challenges the Province to move beyond the scope of privatisation simply for revenue generation purposes. There is a significant opportunity for the Province to undertake sweeping reforms that would see increases in efficiencies, improvements in client services and increases to the fairness of the current wholesale pricing regime. Issues that the ORHMA would like to see addressed in this full-scale review include:

- The elimination of the gallonage fee.
- The introduction of a true wholesale pricing regime for licensees.
- Private warehousing and distribution options.
- Elimination of delivery charges for wholesale customers.
- Off premise licensee sales.
- Streamlining regulations and ensuring liquor inspection consistency and accountability.

Government must strongly encourage the LCBO to modernize its wholesale business. While many of the objectives that the hospitality industry would

like accomplished would not require privatisation, many of them would flow naturally from private sector competition.

**Recommendation:**

**The ORHMA recommends that the Government eliminate the gallonage fee that is based on the unsound principle of charging a tax on a tax.**

**The ORHMA further recommends that the Government undertake a comprehensive review of Ontario's Beverage Alcohol System.**

**Business Meal Deductibility**

Previously, the Association has encouraged the Government to reinstate business meal deductions to previous levels of 100%. Prior to 1988 business meals were fully deductible. Since then, provincial tax deductibility has been reduced to its current level of 50%. The Government should restore the meal deductibility to pre-1989 levels. Restaurants are the boardrooms of small business and at a time when discretionary business spending has been reduced so significantly, such an initiative will assist the hospitality industry by bringing more business guests to their establishments and the wider small business community by providing them with a small measure of retail sales tax relief. This measure allows the Government to encourage business spending and assist the foodservice sector to through these difficult economic times. The fragile nature of the industry is such that the additional business clients that this will allow restaurants to attract may mean the difference between an establishment bankruptcy and remaining in business.

**Recommendation:**

**The ORHMA recommends that the Government increase the current 50% tax deductibility on restaurant meals to its pre-1989 level of 100%.**

**Commercial Property Taxes**

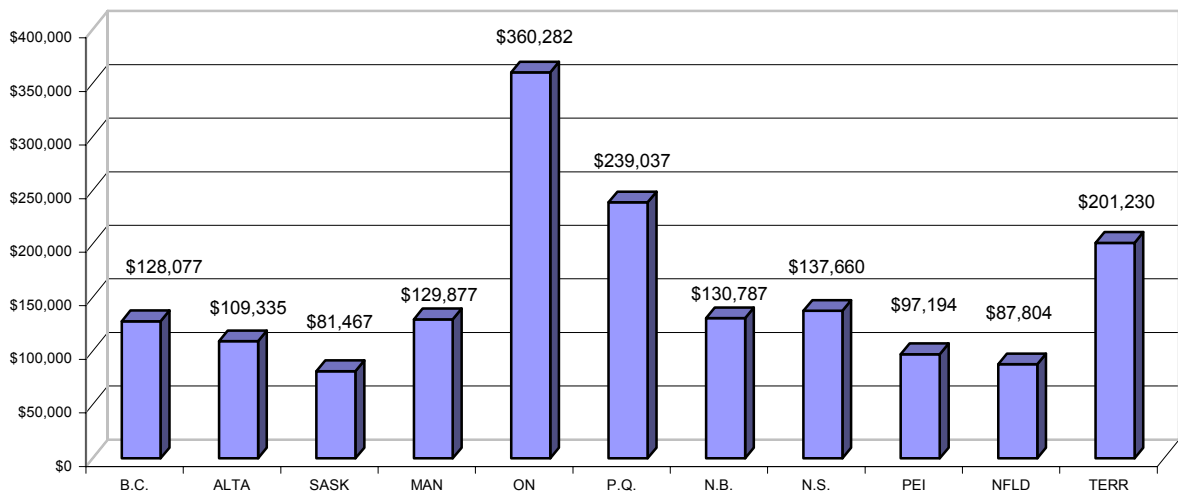
Commercial property taxes in Ontario remain unfairly and uncompetitively high. At a time when municipalities are dramatically reducing services and charging commercial users additional fees for existing services, it is

surprising that property taxes continue to make up 17% of an establishment's net income before tax.

It is valid to ask why commercial property taxes remain unchanged as municipalities reduce service levels and increase user fees for business. For example, in 2002 the City of Toronto began charging user fees for commercial garbage collection. Under their full-cost-recovery model, a small restaurant with approximately 70 seats would be forced to pay \$8500 annually for waste collection, a core municipal service previously funded by commercial property taxes. Not surprisingly, there was no requisite reduction in this restaurant's commercial property tax.

Ontario accommodation properties are equally concerned and already pay the highest amount of property taxes on a per establishment basis when compared to the rest of the country.

**2000 Average Property Taxes  
Paid Per Accommodation Establishment  
Provincial Comparison**



Graph B<sup>9</sup>

As the above graph illustrates, Ontario's accommodation properties pay almost 80% more in property taxes than the national average of \$201,063.

<sup>9</sup> Source: KPMG / Hotel Association of Canada Study

ORHMA's membership was encouraged when the Ontario Legislature passed Bill 140 "Continued Protection for Property Taxpayers Act" into law. This effort to reintroduce fairness into Ontario's Property Tax System was a welcome initiative and will encourage future capital investment in the province.

Unfortunately, many municipalities have done little to move commercial tax rates to within the provincially prescribed 'ranges of fairness'. As a result, commercial property tax, in a vast majority of jurisdictions, continues to cross-subsidize residential services.

Employers are not a limitless source of commercial property tax revenue intended to subsidize residential municipal services. In Ottawa, commercial property tax rates are 2 to 3 times residential rates and in North Bay they are more than 3 times the amount of residential property taxes.

As for municipalities that may seek an exemption from the commercial property tax caps, the Government should not allow these exemptions. The caps should remain in place and at their current level.

### **Recommendation:**

**The ORHMA recommends that, if municipal governments do not immediately begin to take "considerable steps" to move their tax ratios towards the provincially set 'ranges of fairness', the provincial Government introduce further legislation requiring municipalities to reduce commercial property tax ratios and require all municipalities to be within the 'ranges of fairness' by 2006.**

**The ORHMA further recommends that the provincial Government maintain the existing commercial property tax rate caps.**

### **Liability Insurance**

The Association was encouraged by the Government's initiative on the issue of automobile insurance rates. The mandated freeze on insurance premium rates and the subsequent premium rate review was well received by many Ontarians. A similar approach is needed to examine the topic of business liability insurance premiums. Recent and dramatic increases in liability insurance premiums have cut deeply into already razor-thin 5% average after-tax profit margins of our industry.

As an example of the erratic and unmanageable problems that liability insurance premiums are causing: one operator has seen his insurance premiums increase from \$45,000 to \$125,000 in a single year and this is not an isolated occurrence. In fact, business insurance premiums have increased, at minimum, by an average of 25% across the industry. Some operators, with no recent claims, have experienced rate increases up to, and in some cases in excess of, 100% in a single year. These dramatic premium hikes come at an increasingly difficult time for foodservice and accommodation operators. The decreasing number of insurance providers and significantly higher premium rates have forced some operators to run their businesses without insurance thereby risking the long-term security of their businesses and –in some cases- personal assets including retirement savings and family homes. The Government must act to address this issue.

### **Recommendation:**

**The ORHMA recommends that the Government act immediately to introduce a measure of stability into the system by freezing business liability insurance premiums and creating a joint industry-government working group to discuss the issue of business liability insurance to ensure effective competition amongst insurance providers and affordable premium rates for employers.**

### **RST Exemption Threshold From \$4 — \$6**

Given media reports that the Government is considering eliminating this exemption, the ORHMA reiterates the importance of this threshold to both foodservice operators and lower income Ontarians and recommends that the Government increase the threshold exemption from \$4 to \$6.

As you are no doubt aware, meals purchased from a restaurant that are under \$4 are not subject to provincial sales tax. In fact, this threshold was established by David Peterson's Liberal government to provide a measure of relief for lower income Ontarians.

It is not uncommon to see mom 'n pop establishments advertise breakfast, dinner and children specials at \$3.99 (i.e. "\$3.99 bacon & eggs special" or "\$3.99 sandwich & soft drink special"). This PST threshold of \$4 has not been increased since it was established in 1987 and has lost significant value in real terms due to inflation and rising input costs. As such, it now

represents a significant barrier to growth in the struggling foodservice industry.

The \$4 threshold is also not reflective of changing socio-economic circumstances, especially for working parents and their children who eat at restaurants on a regular basis to meet the demands of their busy schedules. Given the unfortunate trend towards 'time poverty', the days when eating away from home was considered a luxury have long since passed, as many segments of the population rely regularly on eating outside of the home. For these consumers who need it most, the threshold no longer provides the intended level of benefit for which it was originally established.

The foodservice industry has first-hand experience in dealing with this highly utilized threshold. Foodservice customers are acutely aware of the \$4 threshold and adjust their spending behaviour accordingly. It is not uncommon to witness families making separate transactions to ensure that their transactions fall under the \$4 threshold.

As a result of this significant consumer awareness, the threshold quickly became a critical pricing point for restaurant operations when it was introduced in 1987. However, over the last 17 years, as food and operating costs have continued to rise, the threshold has remained fixed. This has resulted in a substantial erosion of margins for small independent operators. For meals priced under the \$4 threshold costs are almost at the point of exceeding revenues.

These diminishing margins clearly have a detrimental impact on foodservice establishments and an operator's ability to hire employees and grow their business especially given the current economic climate.

### **Recommendation:**

**The Ontario Restaurant Hotel & Motel Association recommends that the seventeen year-old \$4 RST threshold should be increased to reflect current circumstances for both consumers and foodservice employers.**

### **Employer Health Tax**

The Employer Health Tax (EHT), a highly profit-insensitive tax, has a disproportionately significant impact on labour intensive workplaces such as foodservice and accommodation establishments. Taxes of this nature

punish businesses for having fewer profits while employing more people. The Government should not impose this tax on Ontario's small business community.

The \$400,000 payroll threshold, introduced in 1996, has assisted the hospitality industry in the creation of over 93,000 new jobs. Given the state of Ontario's small, independently owned hospitality businesses, this is not the time to re-introduce this tax as it would damage independently owned and operated hospitality business at a time they are attempting to recover from 2003 losses.

It should be noted that our closest neighbour, to the west, Manitoba has a higher EHT threshold, exempting the first \$1,000,000 of payroll. Introducing this tax on small business would have a significantly detrimental impact on small, largely family-owned hospitality businesses.

**Recommendation:**

**The ORHMA recommends that the Government of Ontario not impose the Employer Health Tax on Ontario's small-business community, but should preserve the \$400,000 exemption threshold.**

## Summary of ORHMA Recommendations

**Recommendation #1:** The ORHMA recommends that, to regain its competitive position in relation to other jurisdictions and to continue its recovery from the economic impact of SARS, the Ontario Government make a strategic, multi-year tourism investment commitment beginning with the allocation of the remaining second-year, SARS recovery investment.

The Association also recommends that the Government continue to support and fully-fund the efforts of the Ontario Tourism Marketing Partnership Corporation and that the OTMP remains as a public-private partnership at arms-length from Ministry of Tourism and Recreation.

**Recommendation #2:** The ORHMA recommends that the Government eliminate the gallowage fee that is based on the unsound principle of charging a tax on a tax.

The ORHMA further recommends that the Government undertake a comprehensive review of Ontario's Beverage Alcohol System.

**Recommendation #3:** The ORHMA recommends that the Government increase the current 50% tax deductibility on restaurant meals to its pre-1989 level of 100%.

**Recommendation #4:** The ORHMA recommends that, if municipal governments do not immediately begin to take "considerable steps" to move their tax ratios towards the provincially set 'ranges of fairness', the provincial Government introduce further legislation requiring municipalities to reduce commercial property tax ratios and require all municipalities to be within the 'ranges of fairness' by 2006.

The ORHMA further recommends that the provincial Government maintain the existing commercial property tax rate caps.

**Recommendation #5:** The ORHMA recommends that the Government act immediately to introduce a measure of stability into the system by freezing business liability insurance premiums and creating a joint industry-government working group to discuss the issue of business liability insurance to ensure effective competition amongst insurance providers and affordable premium rates for employers.

**Recommendation #6:** The ORHMA recommends that the seventeen year-old \$4 RST threshold should be increased to reflect current circumstances for both consumers and foodservice employers.

**Recommendation #7:** The ORHMA recommends that the Government of Ontario not impose the Employer Health Tax on Ontario's small-business community, but should preserve the \$400,000 exemption threshold.