



ONTARIO RESTAURANT HOTEL & MOTEL ASSOCIATION

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

2005 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. This is net of substantial indirect employment as a result of rounds of spending in the economy. 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)
- more than 17,000 establishments licensed with the Alcohol & Gaming Commission Ontario
- 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
- Average pre-tax profit margins within the industry are 4.3% for the foodservice sector and 3.7% for the pub and tavern sector

- The average full-service restaurant contributes more than \$173,200 in taxes annually to all three levels of government
- 17% of an operator's tax burden comes from property taxes

Accommodation Industry Highlights:¹

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

State of the Industry

Ontario's hospitality industry continues to struggle from a number of factors and events over the last few years that have contributed to declining tourism numbers and spending, creating economic instability for many businesses. Events such as 9/11 and the resultant border delays, SARS, BSE, the NHL strike, increased food costs due to weather conditions in the southern States, and the high Canadian dollar are all factors outside the industry's control that have had significant and direct negative impacts on the industry. Uncontrollable rising costs such as gas and oil prices, and insurance costs have also greatly affected the hospitality sector.

These factors have affected the travel patterns into and out of Ontario. U.S. tourists to Ontario accounted for more than 20% of Ontario's tourism in 2004. Only 21 million Americans traveled to Ontario in 2004, compared to 28 million in 2001, a decline of 25%. Tourism projections indicate a slight increase in American tourism to Ontario over the next four years, but 2008 estimates (25 million) remain lower than 2001 statistics.

In 2004, tourism within Ontario, by Ontarians, accounted for more than 73% of Ontario tourism. However, in 2004 more Ontarians chose to travel outside of Ontario over previous years and this trend is projected to continue over the next four years.

In order to support the sustainability of the industry, and grow Ontario's economy, the Government must take action to ensure that both fiscal and social policies foster and

¹ (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.)

support business growth, and do not jeopardize investment, competitiveness and employment.

In November, the Government introduced amendments to the Labour Relations Act. These amendments will fundamentally shift the balance in union certification drives, will threaten employees' fundamental right to vote, and affect an employer's fundamental right to freely communicate with its employees. This will impact labour relations, the balance in the workplace, and will influence the investment decisions of many companies.

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

Beverage Alcohol Reform

The ORHMA was very pleased with the announcement made last week by the Finance Minister that the Government has established a panel to undertake a comprehensive review of Ontario's beverage alcohol system. The Association has been seeking such a review for quite some time, and looks forward to the opportunity to work with the Minister's advisory panel in representing the concerns of the licensee community.

Ontario's liquor sales licensees are caught in a complex web of provincial fees, mark-ups, levies and taxes as the price of doing business. Some are required to operate while others are embedded in the price of the beverage alcohol product. Both types result in driving up licensee costs and cutting into slim profit margins. For example, to enter the business, a potential licensee must initially submit a completed application to the Alcohol and Gaming Commission of Ontario with payment of a one-time, non-refundable fee of:

- \$1,055 if public notice is required i.e. the premises has not previously been licensed or the premises has not been licensed for the past six months; or
- \$925 if no public notice is required.

Upon issuance, the license is valid for 2 years at which time the AGCO asks for another \$450 up-front for renewing the license for a further three years.

Over and above the application fee and before the license is issued, the applicant may also have to pay for newspaper advertising (if public notice is required), the hiring of a professional engineer or architect should municipal building or fire refuse to provide a capacity calculation, and server training of management and staff.

By regulation, liquor sales licensees must purchase beer, wine and spirits for resale to the public from a "government store" under their license and maintain any receipts on their retail site for inspection. A "government store" for purposes of regulation can be a government owned-and-operated LCBO retail store or privately owned and operated Brewers Retail Inc. outlet (the Beer Store) or other retail store that has been authorized by the LCBO to sell on its behalf.

By pain of severe sanction, licensees cannot purchase and have on their premises any liquor not purchased under their license from a government store and must show liquor receipts to an AGCO inspector on request.

Prices to liquor licensees for beverage alcohol can end up being greater than those offered to the public due in large part to the imposition of the "gallonage fee". The regular shelf price paid by a consumer for beer, wine and spirits reflects a myriad of different fees, levies, mark-ups and taxes imposed by the provincial and federal governments on a supplier's product. Although licensees do receive a small LCBO discount, the "gallonage fee" takes away any price advantage.

Although the "gallonage fee" is found in the AGCO's Schedule of Fees, it is collected by the LCBO. The tax is based on volume for beer and price for wine and spirits:

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

On resale to customers, a licensee must collect and remit a further 10% provincial sales tax. This cumulative application of myriad fees, levies, mark-ups and sales taxes has a compounding effect and serves to make licensee beverage alcohol prices to patrons artificially high in comparison to a structure that would be based on a wholesale price structure. This is basically a tax on a tax. Because licensees have no buying options when it comes to purchasing beverage alcohol, establishing a true wholesale pricing regime for licensees and removing the gallonage fee would provide relief to a sector characterized by dramatically falling revenues, rapidly rising costs and increasingly thin profit margins.

- **The ORHMA recommends that the government eliminate the gallonage fee on licensee sales that is based on applying one sales tax on top of another.**
- **The ORHMA also recommends that the government implement a true wholesale pricing regime for liquor sales licensees.**

The ORHMA has a further concern with the state of competition within the domestic beer industry and, more specifically, the lack of any regulatory oversight over domestic beer pricing. Because Ontario's beer market is a duopoly, government must maintain a role to ensure the beer market remains competitive and any price increases can be justified by domestic brewers.

Until a few years ago, brewers had to provide just such a rationale before the LCBO would entertain any price changes. This was replaced by a reporting system whereby brewers simply registered price changes with the LCBO that would go into effect within two weeks.

- **The ORHMA recommends that the government establish a transparent and accountable system for beer pricing in Ontario that fosters more competition, more selection and more purchasing options for the licensee community.**

Within the one organization - the Alcohol and Gaming Commission of Ontario - reside the roles of enforcer, adjudicator and administrator of sanctions. Although the enforcement and prosecution of licensees who are in violation of the Liquor License Act are functions performed by AGCO staff, while hearings adjudication and imposing of sanctions rest with the AGCO's government-appointed members of the Board of Directors, both functions reside within the same organization.

Over the past several years, case law has stressed a strict segregation between the roles of enforcer/prosecutor and adjudicator to prevent apprehension of bias and to promote the tenets of natural justice. The legal requirements to sustain such a distinction grow more onerous. There have even been legal challenges that approach the question of bias when a government in power itself appoints adjudicators for terms. To alleviate any perception of bias and ensure a clear distinction of roles, the ORHMA recommends the further separation between the role of enforcement/prosecution and the adjudicative role.

- **The ORHMA recommends that government separate the enforcement/prosecution function from the adjudicative function of the AGCO when addressing disciplinary actions against liquor licensees.**
- **The ORHMA further recommends that the government examine a staged approach to compliance with the Liquor License Act, including a range of options and sanctions.**

Smoke-Free Ontario Act

The Ontario Tobacco Strategy has focused energy and resources on assisting individuals to quit smoking, and has dedicated aid to tobacco farmers to prepare them for a smoking ban, but has not examined efforts to assist the hospitality industry in preparing for the implementation of the Smoke-Free Ontario Act. Our industry is already suffering, and we require and deserve the government's attention on this matter.

For the past number of years there has existed a patchwork of municipal smoking by-laws throughout the province. The ORHMA has supported the introduction of provincial legislation to do away with that patchwork and to create a level playing field for the industry. However, the ORHMA has consistently called on the Government to include a provision in the legislation that would permit separately ventilated Designated Smoking

Rooms (DSRs) to operate, with safeguards for staff, and was disappointed that such a provision was not included in the legislation which, if passed, would result in the closure of all designated smoking rooms by May 31, 2006.

Across Ontario more than 700 business operators have invested heavily in the establishment of separately ventilated, municipally-approved DSRs. Many of these DSRs were built to comply with June 1, 2004 changes to smoking by-laws in Toronto, Mississauga, Brampton and York Region. In every case, operators have made a significant investment on the understanding that they would recoup their substantial capital expenditures over a payback period of many years.

The Smoke-Free Ontario Act, if passed without amendment would leave these operators, the majority of them independent, without any financial recourse. The investments they have made to date are significant, and the closure of the DSRs in 2006 will directly and immediately threaten their businesses. With an already weakened financial climate within the industry, due to numerous factors listed above, many of these operators will have no choice but to close their doors unless there is some assistance from the Government. The operators in Ontario who have invested in DSRs require assistance from the Government to help them recoup investment.

Although the recommendation is specific to operators who have invested in a designated smoking room the Government must keep in mind that many jurisdictions in Ontario currently do not have municipal by-laws that restrict smoking in restaurants and bars. Operators in these areas too will certainly suffer an immediate if not permanent loss of business when the Smoke-Free Ontario Act comes into effect.

Smoking bans have a severe affect on bars and taverns, much more so than on restaurants, and this past year when a smoking ban came into effect in New Brunswick more than 70% of operators reported an immediate decline in business as a result within the first two months.

In Ontario, based on the current business climate in the industry many operators fear that due to municipal smoking by-laws they will not be able to keep their doors open until the provincial legislation comes into effect.

Tavern, bar and nightclub operators in Ontario saw their sales plummet by 17.6% between 1999 and 2003 – a loss in sales of \$106,700 for the average operator. The trend continued through the first quarter of this year with another 7.4% drop. In another indicator of a tough business climate, profit margins for bar, tavern and nightclub operators in Ontario have shrunk from 6.5% of operating revenue in 2001 to just 3.7% in 2002, the most recent year for which data are available.

- **The ORHMA recommends that the Government prepare a phase-out strategy for the hospitality industry, as it has done with cessation programs for individuals who want to quit smoking and strategic initiatives to support the farming community. The hospitality sector phase-out strategy may**

include such supportive measures as the elimination of the gallonage fee, and the establishment of a wholesale liquor pricing structure.

- **The ORHMA further recommends that the Government provide compensation, possibly in the form of accelerated depreciation schedules, one-time lump sum payment, or the opportunity for more revenue generation, to the more than 700 operators who have invested in municipally approved Designated Smoking Rooms.**

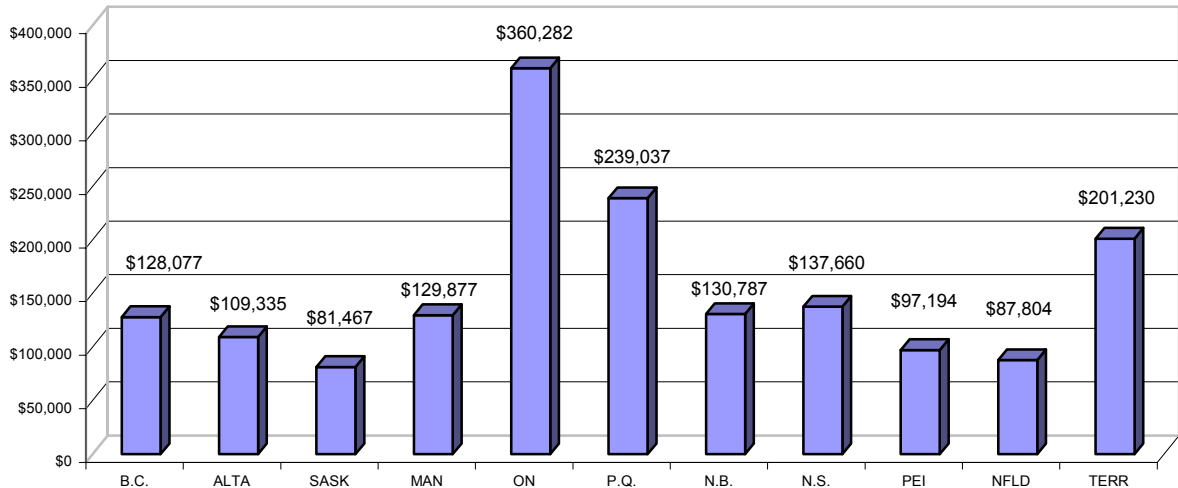
Taxation Policy

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 B²

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

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.

The hospitality industry currently contributes significantly to municipal revenues and objects to any further powers of municipalities to levy additional fees. Profit margins in

² Source: KPMG / Hotel Association of Canada Study

the hospitality industry, after tax, are below 5% on average. Additional taxes and levies will only cut into profit margins further and will impede new investors and entrepreneurs hoping to open a new business, and will result in the loss of revenues and thereby the loss of jobs. The provincial government must bear this in mind and must not permit new powers of revenue generation to municipalities.

- **The ORHMA recommends that the provincial Government introduce further legislation requiring municipalities to reduce commercial property tax ratios and require all municipalities to be within the range of fairness by 2006.**
- **The ORHMA further recommends that the provincial Government maintain the existing commercial property tax rate caps.**

Investment in Tourism

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 only lead to long-term losses in economic activity, employment and government revenue.

Research-based marketing campaigns are necessary, but also beneficial, as witnessed by the Tourism Revitalization Program, administered through the OTMPC, which returned \$8.40 on every dollar invested.

Dedicated investment in tourism marketing is fundamental to the success of the tourism and hospitality industries. The Ontario Tourism Marketing Partnership Corporation works collaboratively with the private sector to promote Ontario as a four-season destination through the development of research-driven campaigns.

- **The ORHMA recommends that the Government support the promotion of tourism within and to Ontario through a \$20 million increase in permanent annual funding to the Ontario Tourism Marketing Partnership Corporation.**

Another effective method of supporting tourism marketing is through Destination Marketing Fees. The ORHMA supports industry-initiated Destination Marketing Fees to help the tourism industry toward its goal of attracting tourists and tourist spending and achieve economic renewal. The ORHMA supports a DMF based on the principles that the introduction of a DMF be:

- a voluntary, industry-initiated decision;
- that the funds generated be dedicated to destination marketing and tourism promotion;

- that the amount of the DMF not exceed 3% of the cost of a hotel room;
- that the DMF be transparent and clearly indicated on customer billing; and,
- the Government makes permanent the PST exemption on Destination Marketing Fees.

In the 2004 provincial budget the Government announced a one-year exemption from retail sales tax for DMFs. With a positive return on investment DMFs generate increased direct and indirect revenues with a greater economic impact than retail sales tax. For this simple reason the ORHMA recommends that the Government make permanent the retail sales tax exemption on Destination Marketing Fees.

- **The ORHMA recommends that the Government make permanent the Retail Sales Tax exemption on Destination Marketing Fees.**
- **The ORHMA further recommends that the Government reject municipal requests to levy a hotel room tax to fund municipal infrastructure and programming costs, or any other amendment to the Municipal Act and the City of Toronto Act that would establish any further power of municipalities to levy fees and place additional financial burden on the business community.**

Waste Diversion Ontario

The ORHMA is concerned with the current status of Waste Diversion Ontario. Under the Waste Diversion Act several Quick Service Restaurant (QSR) chains are obligated to remit levies annually to fund their share of 50% of the cost of municipal blue box programs.

When steward fees were announced just two years ago they were estimated at \$30 million. This estimate was quickly revised to \$42 million. Now, just three years into the program Steward fees for 2005 have just been approved at \$64.3 million. Stewardship Ontario has further indicated that these fees are expected to continue to rise in the next years. The rate and amount of fee increases makes both the ability to pay these fees and support for Waste Diversion unsustainable.

The Minister of Environment indicates that these new fees represent 50% of the costs of municipal blue box programs. Industry stewards are seriously concerned that municipalities have not implemented cost containment strategies and have no incentive to do so. Further, there is no accountability whereby stewards are assured that the funds submitted actually are directed toward the operation of blue box programs. These concerns have all also been expressed by the Environment Commissioner, and as yet have gone unaddressed by the Ministry.

The ORHMA is seeking assurances that the funds submitted are directed to the operations of blue box programs, and that municipalities work toward running more efficient operations, whether that be by operating better programs municipally, or merely negotiating a leaner and more efficient contract to a third party.

- **The ORHMA recommends that the Government establish a standard municipal model for waste diversion, specifying the types of materials collected and the costs and revenues associated with each, as well as a standard reporting model, to assure Stewards that remitted funds are directed to approved costs and expenditures.**
- **The ORHMA further recommends that using the standard municipal waste diversion model the Government compel municipalities to implement cost containment strategies.**

Summary of ORHMA Recommendations

- **The ORHMA recommends that the government eliminate the gallonage fee on licensee sales that is based on applying one sales tax on top of another.**
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