Sign companies seeking clarity on indirect taxes at SCC

Billboard battle looms

Monday, June 25, 2012 | Written by Glenn Kauth |

Toronto's billboard-tax battle isn't over yet as the losing parties in the matter before the Ontario Court of Appeal are attempting to take the case to the Supreme Court of Canada.

Toronto's sign levy is 'incredibly burdensome,' says Patrick Harrington.

"As municipal governments exercise their new taxing powers to expand revenues, it becomes increasingly apparent that these tests, indicia, and approaches require revision and clarification," lawyers for the applicants, the Out-of-Home Marketing Association of Canada and Pattison Outdoor Advertising LP, wrote in their May 31 application for leave to the Supreme Court of Canada.

The case centres largely on the distinction between direct and indirect taxes. Municipalities don't have the power to levy indirect taxes, which the applicants argue Toronto's sign levy amounts to in that it causes those who own and control the advertising copy to pass on the added costs to advertisers through higher rates or to landowners in the form of lower lease payments.

Patrick Harrington, a partner at Aird & Berlis LLP in Toronto, notes the courts have long struggled to deal with the distinction between direct and indirect taxes.

Essentially, the issue comes down to whether the people charged a levy are the ones who pay it — which makes it a direct tax — or whether someone else will end up reimbursing them.

The City of Toronto, by imposing a levy of between $1,150 and $24,000 per year (based on the type and aggregate face area) on those who own and control the sign copy, argued it was taxing the sign operators through a direct tax.

But the applicants for leave at the Supreme Court argue that as the tax is equal to or exceeds the profits earned, owners would therefore have to pass on the costs to advertisers.

But in writing the ruling on the issue in *Out-of-Home Marketing Association of Canada v. Toronto (City)* [http://canlii.ca/en/on/onca/doc/2012/2012onca212/2012onca212.html] on April 2, Ontario Court of Appeal Justice Robert Sharpe saw things differently.

The classic economic distinction between direct and indirect taxes, he noted, comes from John Stuart Mill: "Indirect taxes are those which are demanded from one person in the expectation and intention that he shall indemnify himself at the expense of another: such as the excise or customs."

But, according to Sharpe, case law has established "that the legal definition of an indirect tax is not to be determined on the basis of pure economics or on the basis of the particular financial circumstances of the parties affected by the tax.

The reason is obvious: if the argument of Pattison and OMAC were accepted, virtually every tax would be an indirect tax. Every business that bears a tax will treat the tax as a cost that must be factored into the price charged for its products."

Sharpe went on to look at whether the tax relates to the price of or the revenue from advertising. He concluded that it doesn't. "It is a flat annual tax imposed on the sign owner," he wrote.

"It is not a tax on the commodity sold by the sign owner and it is not imposed on, rated or rateable to a unit of the commodity or its price.

It is not imposed on a commodity in the course of production or marketing and therefore it cannot 'cling' as a burden to the unit or transaction as it is presented to the market."

Sharpe added: "To repeat, the annual tax at issue here may increase Pattison's and OMAC's cost of doing business and those parties may therefore charge more for the product they sell.

However, the annual tax is not imposed on a unit of advertising space sold by the appellants and it lacks the 'clinging' quality that is the hallmark of an indirect tax."

But Harrington, who had been involved with the issue at the earlier stages, notes the need for clarity on the issue given the multitude of tests that are out there and as the Supreme Court hasn't dealt with the question of indirect taxes for several years.

In this case, he suggests, the judges had likely already decided what the outcome would be and then could "simply pick the test or the criteria that will get them to that result."

Harrington suspects the appeal court was looking for a way to validate the sign tax. "We all know that the city is in desperate need of revenue," he says.

For their part, the sign companies seeking leave propose a single test for indirect taxes: "In light of the context and purpose of the tax, is the general tendency of the tax such that it will be passed on? If yes, the tax is an indirect tax."

The issue has other implications as well, according to Harrington. He notes he has other clients that face various municipal fees and would like to know if they're in fact valid. Other municipalities also likely have interest in the case.

If the top court upholds the sign tax, other towns and cities might seek similar powers to Toronto's, says Harrington. "It's incredibly burdensome," he says of Toronto's levy.

"It has forced the removal of lawful signs," he adds, noting the tax was part of a regulatory strategy "to dissuade new signs from being erected."

Harrington also refers to another issue that surfaces in the applicants' grounds for seeking leave to appeal at the Supreme Court: "If you tax a sign where it's now uneconomical to operate it, have you interfered with freedom of expression?"

The issue here centred in part on whether the city could apply the tax to existing signs given a provision under s. 110 of the City of Toronto Act stating that a "city bylaw respecting advertising devices, including signs," doesn't apply to those already up.

The Court of Appeal determined that provision didn't apply to the tax, but the applicants for leave are insisting otherwise in arguments that refer to the right to freedom of expression under s. 2(b) of the Charter of Rights and Freedoms.

"Both commercial and non-commercial signs foster political and social decision-making, one of the values underlying s. 2 (b) of the Charter," the application states.

"Because the sign tax affects expressive content, s. 2(b) of the Charter requires that s. 110 be interpreted so as to protect the applicants' existing signs that display commercial and other forms of expression.

Contrary to the Court of Appeal's decision, the powers of a municipal government should not be interpreted in a 'generous fashion' when doing so conflicts with the specific regulatory authority granted to the municipality and in circumstances where the tax negatively impacts freedom of expression."

The third area of appeal deals with the city's exemptions for sign owners that have entered into revenue-sharing agreements with it.

On this score, the applicants were attacking that exemption as it applies to one of Pattison's competitors, Astral Media Outdoor, under which the latter supplies street furniture in exchange for selling advertising on it. The city receives a share of the advertising revenue in turn.

Pattison has complained the exemption gives Astral an unfair advantage since it doesn't pay the tax.

The Court of Appeal, however, rejected that argument given a provision under s. 267 of the City of Toronto Act that allows the city to provide exemptions from taxes.

"The fact that this arrangement may give Astral a competitive advantage over Pattison renders neither the bylaw nor the exemption vulnerable to attack," wrote Sharpe.

"The revenue-sharing agreement with Astral is simply a different arrangement, fully authorized by the act and the bylaw, that permits Toronto to advance and achieve legitimate municipal objectives."

The sign companies, however, see it differently. "In the instant case, the exemption from taxation for a third-party sign

owner who has entered a revenue-sharing agreement with the City of Toronto is discriminatory," the application for leave states.

"The exemption creates two classes of signs in Toronto: those on private property that are taxed; and those subject to a revenue-sharing agreement with the city that are not taxed."

The applicants argue that while the city can differentiate between groups or classes of citizens, "it is not permissible for the city to self-deal" through an exemption for Astral that the objecting sign companies claim will ultimately result in increased revenues for the municipality itself. The arrangement, they assert, amounts to a "pernicious form of discrimination."

Harrington expresses similar concerns. "There's just something that smells bad" about the city exempting the companies it has contracts with, he says.

But Kim Mullin, co-chairwoman of the municipal and planning law practice at WeirFoulds LLP, says the courts and the legislation have moved more towards allowing towns and cities to allow for such distinctions and exemptions.

"The case is entirely consistent with the direction the law has been going in over the last number of years," she says in reference to the appeal court's ruling.

The courts, she notes, have moved away from a tendency to overturn municipal decisions and bylaws in favour of a more deferential approach.

At the same time, she adds, provincial legislation governing municipalities has followed that trend by specifically allowing them to differentiate in applying bylaws.

Toronto, of course, isn't the only city that has imposed sign taxes. Montreal, for example, has its own levy. But according to Harrington, the latest legal wranglings are a signal that the debate continues.

"It's an interesting one in the way that it has captured constitutional and Charter issues in ways that might not be expected," he says.