Corporate Planning and Financial Services Report to Executive Committee
2022 September 29

ISC: UNRESTRICTED
EC2022-0780

Non-Residential Assessment Subclasses Scoping Report

RECOMMENDATION(S):

The Executive Committee recommends that Council direct Administration to continue advocacy for enabling legislation that provides expanded flexibility on non-residential subclasses.

RECOMMENDATION OF THE EXECUTIVE COMMITTEE, 2022 SEPTEMBER 29:

That Council direct Administration to continue advocacy for enabling legislation that provides expanded flexibility on non-residential subclasses.

Excerpt from the Minutes of the Regular Meeting of the Executive Committee, dated 2022 September 29:

"**Moved by** Councillor Walcott

That with respect to Report EC2022-0780 the following amendment be approved:

That the Executive Committee forward this item to the 2022 October 4 Combined Meeting of Council as an Item of Urgent Business.

For: (9): Mayor Gondek, Councillor Spencer, Councillor Penner, Councillor Pootmans, Councillor Walcott, Councillor Chu, Councillor McLean, Councillor Sharp, and Councillor Wyness

MOTION CARRIED"

HIGHLIGHTS

- Administration has prepared the attached scoping report in response to Financial Task Force recommendation #26 which directed Administration to investigate how non-residential subclasses may be used to mitigate tax distribution changes, including to support targeted, temporary tax relief.
- **Reason for Recommendation:** Although subclasses are not recommended to address market volatility, continued advocacy is recommended because expanded flexibility in non-residential subclasses could be useful in other circumstances to provide targeted tax relief or incentives in support of other public policy objectives which should be considered on a case-by case basis with respect to the costs and benefits they may create.
- While non-residential assessment subclasses could be used as a strategy to address tax volatility resulting from changes in assessment values by redistributing tax responsibilities from some non-residential properties to others, Administration is recommending against using this tool to address more narrow situations like the downtown tax redistribution because:
  - A subclass in itself does not mitigate tax volatility; Council would need to set additional tax rates annually to decide which properties should receive tax relief, how much tax relief should be provided, and which properties should subsidize that relief;
  - A subclass designed to address the downtown tax redistribution would have primarily redistributed tax responsibility to property owners and businesses with

reduced ability to pay, which would be in direct conflict with The City's Downtown Strategy;
  - Subclasses can still result in a "bow wave" when assessment values stabilize; and
  - Implementation of subclasses would increase system complexity and significantly increase costs associated with tax administration and communication to property owners and businesses.
- **What does this mean for Calgarians?** A non-residential subclass in effect between 2015 and 2021 would have had the unintended effect of increasing costs for businesses experiencing a decreased ability to pay. Other uses of non-residential subclasses could potentially be more effective at helping The City achieve strategic objectives beyond the remedy of a tax issue.
- **Why does it matter?** Financial Task Force recommendations seek to ensure more sustainable, long-term approaches to municipal fiscal issues. It is important to conduct significant research, public consultation, and values-based analysis to proactively identify potential impacts and ensure a subclass will achieve desired outcomes.
- Strategic Alignment to Council's Citizen Priorities: A prosperous city and A well-run city
- Background and Previous Council Direction is included as Attachment 1.

DISCUSSION

Pursuant to Financial Task Force recommendation #26, the attached scoping report investigates the impacts of implementing non-residential assessment subclasses as a strategy to mitigate tax distribution changes, including to support targeted, temporary tax relief. Non-residential subclasses are used by some jurisdictions to reduce volatility in tax responsibility for those experiencing significant year over year increases in their assessed property values. Subclasses divide up a property assessment class to intentionally re-distribute municipal property tax responsibility from one group to another within a class, but they are not designed to change municipal tax revenues overall in a revenue neutral system. Importantly, the non-residential subclass options available to Alberta municipalities under the current legislation are highly restricted and none would serve as a viable option for reducing tax volatility or for providing effective targeted tax relief. Enabling legislation would be required before non-residential subclasses could be implemented for this purpose in Calgary.

In preparing the attached scoping report, Administration investigated various subclass techniques used across Canada to determine whether Calgary should pursue the legislative authority to implement such methods to provide temporary tax relief. To understand if non-residential subclasses would be a useful tool to mitigate the negative impacts of tax volatility in Calgary, Administration conducted research and analyzed historical data to test if subclasses based on property type, geographic location or business type could have addressed the impacts of the significant downtown tax redistribution that gave rise to the Financial Task Force Report.

This investigation shows that non-residential subclasses could potentially be useful and reduce costs for targeted properties; however, there are significant costs and limitations to be considered in weighing if subclasses are the best tool to address tax redistribution problems. When deployed to mitigate impacts of market volatility, non-residential subclasses require those who are experiencing assessment decreases, or a loss in property value, to directly subsidize those who are experiencing assessment increases, or a gain in property value. In Calgary, office properties saw the most dramatic decreases between 2015 and 2021, and while their assessed values reflected a likely decrease in income potential, non-residential subclasses that could have provided tax relief to the properties that experienced tax increases would have forced these office properties to bear a larger share of tax responsibilities than what their current market values dictated. This manipulates the market-based valuation system in place today and creates horizontal and vertical inequities (i.e. those with same market values could hold different tax responsibilities and those with different market values could hold similar tax responsibilities). Further, if implementing non-residential subclasses, Council would need to consider alignment with other objectives and strategies during considerations for program design.

Additionally, while non-residential subclasses offer support to those adversely impacted by tax volatility, it could lead to an overall increase in administration costs due to loss of efficiency and expanded property owner communication, thereby requiring an increase in the overall revenue required from property taxes.

Furthermore, Alberta has a relatively simple taxation system compared to other jurisdictions across Canada. Adjusting this system would require taxpayers to learn a new system while increasing the complexities of the calculations required to ascertain tax responsibilities. This not only harms the simplicity principle but could cause taxpayers to incur costs as they come to understand and learn to navigate the new system.

In addition, the market volatility that Calgary experienced between 2015-2021 has mostly stabilized. While non-residential subclasses could potentially address the volatility challenge raised by the Financial Task Force Report and could have mitigated the impact of the downtown tax redistribution, implementing non-residential subclasses now for that purpose would likely add costs with minimal benefits and could have the unintended consequence of exasperating the issue that it is trying to address and by creating inequities among taxpayers.

As a tool to set differential tax rates, subclasses may be useful in other circumstances as a tool to provide tax incentives, subsidies, or relief to achieve desired public policy objectives. Potential use of subclasses should be considered on a case-by-case basis following detailed cost-benefit analysis. Enhanced flexibility to create non-residential subclasses would give The City an additional tool that could be used to respond to Calgary’s local context.

STAKEHOLDER ENGAGEMENT AND COMMUNICATION (EXTERNAL)

☐ Public Engagement was undertaken

☒ Public Communication or Engagement was not required

☒ Public/Stakeholders were informed

☒ Stakeholder dialogue/relations were undertaken

Public communication or engagement was not required for the drafting of this report; however, both the Financial Task Force Technical Committee, comprised of experts internal to The City and The Financial Task Force Implementation Steering Committee, comprised of experts internal and external to The City, have been informed of the findings of this report and were consulted in the drafting of this report.

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Administration has also had high level conversations with external stakeholders including the Building Owners and Managers' Association (BOMA) Calgary, NAIOP Calgary, the Calgary Chamber, and representatives from some local tax agencies on the concept of non-residential assessment subclasses. While stakeholders understand the intent of non-residential subclasses, many raised concerns around the complexities this adds to the current tax system, which is generally considered to be simple and transparent for taxpayers relative to other jurisdictions.

IMPLICATIONS

Social

Property taxes have a direct impact on services provided by The City to all Calgarians. The findings of this report highlight alternative approaches to a property assessment system that could mitigate sharp increases in property taxes for some taxpayers at the cost of other taxpayers.

Environmental

Not Applicable

Economic

The attached scoping report explores the costs of implementing non-residential assessment subclasses to mitigate negative impacts of market volatility in Calgary's economy. A subclass designed to mitigate the 2015-2021 downtown tax redistribution would have redistributed tax responsibility to downtown properties that may have less ability to pay.

Service and Financial Implications

Other: The Recommendation does not have any Financial Implications

Implementing non-residential subclasses would require additional resources to communicate, administer and increase the cost of the Property Assessment and Taxation service lines if implemented. Capital funding for technological upgrades will also be required. Early and conservative estimates of the required capital investment for the Assessment software upgrades required to administer non-residential subclasses suggest that that the costs could be up to $575,000. This is a class 5 cost estimate and actual costs may be significantly different. Additional capital funding would be required to update Tax software. However, the estimated capital funding required to update the Tax software would be contingent on the upgrades to the assessment systems because the subclass functions would need to be integrated.

RISK

Although subclasses could be a useful tool in some contexts, subclasses, especially those designed to address market volatility, come with risk to The City.

Complexity and Fairness of the Tax System: Subclasses would increase complexity in the assessment system and redistribute property tax responsibility to those that may have less ability to pay. This may lead to increased dissatisfaction with the property assessment and tax

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system for taxpayers who are directly and indirectly impacted and may lead to an increase in assessment complaints.

Legislative Uncertainty: Currently, the non-residential subclass options available to Alberta municipalities under the current legislation are highly restricted and none would serve as a viable option for reducing tax volatility or for providing effective targeted tax relief. To implement non-residential subclass options that could provide effective tax relief, The City would first have to advocate for and obtain enabling legislation. To the extent that subclasses may be useful in different circumstances to achieve other public policy objectives, the current legislative constraints create risk that The City will not have the tools it needs to be responsive to local needs and interests in the future.

Economic Neutrality: The use of non-residential subclasses for targeted tax relief could reduce economic efficiency as it could lead taxpayers to invest more heavily in the subclass with lower tax rates than in the subclass with higher tax rates or even incentivize property owners and/or their tenants to relocate to other jurisdictions.

Reputation: Subclasses generally reduce transparency and make the assessment system more difficult to understand. If non-residential subclasses were implemented, it would be more difficult to communicate how the system works to the public and some taxpayers may view the change negatively.

ATTACHMENT(S)

1. Attachment 1 - Previous Council Direction, Background
2. Attachment 2 - Non-Residential Subclasses Scoping Report
3. Attachment 3 - Property Type Subclass Illustrative Examples
4. Attachment 4 - Location Subclass Illustrative Examples
5. Attachment 5 - Small Business Subclass Illustrative Examples
6. Attachment 6 – Presentation: Non-Residential Assessment Subclasses Scoping Report

Department Circulation

General Manager/Director	Department	Approve/Consult/Inform
Male, Carla	Corporate Planning & Financial Services	Approve
Lee, Edwin	Assessment & Tax	Approve
	City Manager’s Office	Consult