Revenue Neutral Tax Explanation

What does revenue neutral mean?

Annual property assessment changes are revenue neutral, which means they have no impact on the total property tax amount that The City might raise. Rather, these changes provide for a redistribution of property taxes within Calgary, based on the value of the property owned. Revenue neutral is a term that means the revenue collected through the assessment process will be the same regardless of changes in property values. If market values increase then property owners will not be asked to pay more taxes through the annual assessment process, nor will property owners pay less should values decrease. The revenue neutral process helps explain how an individual property's taxes have changed due to that property's year-to-year change in assessment. Each property's change in taxes, using the revenue neutral tax rate, occurs because the process of assessing properties each year results in taxes being re-distributed among properties. Changes in The City's property tax revenues are thereby communicated within the budgetary process, leading to two distinct and separate assessment and budgetary processes, each transparent and fair.

Why is Revenue Neutral Important?

The City's revenue neutral tax system is consistent with principles in the *Municipal Government Act* (MGA) and guidance from Alberta Municipal Affairs. This ensures that:

- The City does not collect more than it needs from taxpayers
- Total tax revenues do not change automatically with assessment changes year over year, which creates less volatility; and
- Any tax revenue change brought forward by The City is communicated separately through the budgetary process.
- Ensures no new taxes will be collected due to the annual reassessment process
- Creates taxpayers' confidence in the integrity and transparency of the property assessment and tax system.

Conversely, in a rate-driven tax system, assessment value increases or decreases directly impact the amount collected through property taxes.[1] In this system, the assessment is not only responsible for distributing property taxes but controls the magnitude of property taxes as well.[2] This system fails to meet the test of open and transparent property taxation.[3]

The revenue neutral tax system makes certain that the assessment process remains a distinct and separate process from the budgetary process. Revenue neutral ensures that no new taxes will be collected due to the annual reassessment process.

[1] See International Association of Assessing Officers. "Standard on Property Tax Policy." *International Association of Assessing Officers*, 2020: s. 6.2. https://www.iaao.org/media/standards/Standard_on_Property_Tax_Policy.pdf.
See also International Association of Assessing Officers. "Standard on Property Tax Policy." *International Association of Assessing Officers*, 2010: s. 5.2.1.
[2] Ibid.
[3] Ibid.

Revenue Neutral and the Municipal Property Tax Rate Calculation

Once all properties are reassessed and the assessment roll is finalized, a revenue neutral tax rate is determined.

$$\text{Municipal Revenue Neutral Tax Rate} = \frac{\text{Prior Year's Tax Revenue Budget}}{\text{Current Year's Total Assessment} - \text{Physical Growth}}$$

Assessment increases due to physical growth such as new construction is removed from the calculation to ensure that changes in assessed value due strictly to overall market conditions do not generate additional tax revenue, although individual properties may see taxes redistributed.

When property values go up, the revenue neutral tax rate decreases and when property values go down, the rate goes up.

Council sets the budget to ensure that The City collects only what it needs to meet its financial commitments: the operating and capital costs of serving a community of more than one million people. To get the amount of revenues required from property taxes, The City takes the overall expenditure and subtracts all other sources of revenue such as license fees, user fees and provincial grants. The remainder is the amount of money the municipality needs to raise through property taxes in order to provide services for the year. This revenue requirement is then used to calculate the tax rate in accordance with section 355 of the MGA. Any changes in the revenue requirement is applied to the revenue neutral tax rate. Or simply, the tax rate calculation is as follows:

$$\text{Municipal Tax Rate} = \frac{\text{Current Year's Tax Revenue Budget}}{\text{Current Year's Total Assessment}}$$

The tax rate is then applied to each individual property assessment using the following formula:

Property Assessment ($) x Municipal Tax Rate = Municipal Taxes Payable

Because of this revenue neutral approach, taxpayers are assured that The City does not:

- take advantage of rising market values to collect more tax than it needs, or
- calculate property taxes based on the increase or decrease in market value from one year to the next.

In surveying other jurisdictions across Alberta and Canada in 2020, all who have responded have confirmed the use of the revenue neutral system:

Municipality	Taxation Method
Calgary	Revenue Neutral
Camorse	Revenue Neutral
Edmonton	Revenue Neutral
Lethbridge	Revenue Neutral
Red Deer	Revenue Neutral
Grande Prairie	Revenue Neutral
St. Albert	Revenue Neutral
Strathcona County	Revenue Neutral
Medicine Hat	Revenue Neutral
Airdrie	Revenue Neutral
RM Wood Buffalo	Revenue Neutral
British Columbia - Province Wide	Revenue Neutral
City of Winnipeg	Revenue Neutral
City of Saskatoon	Revenue Neutral
Ontario (MPAC) - Province Wide	Revenue Neutral

Though the revenue neutral system is not required, many jurisdictions choose to use it as it provides confidence in the integrity and transparency of the property assessment and tax system.

Within Calgary, the revenue neutral calculation takes place on an annual basis with the finalization of the assessment roll in November. Should The City's property tax budgetary requirements change, the tax rate is further adjusted, typically in spring of each year, to bring in the amount of revenue needed as directed by Council when the property tax bylaw is approved.

How does this work for the average residential homeowner and business owner?

In addition to the revenue neutral tax rate calculation applied to The City's overall tax base, a revenue neutral process is applied to the assessment classes (residential, non-residential and farm land) so that for every additional tax dollar levied to one property, there is a tax dollar reduction in another. Assessment acts only as a mechanism to annually distribute taxes to each taxpayer in an equitable manner. The assessment process does not determine the overall level of taxation, the approved budget does. This is revenue neutrality in action.

The City begins by revaluing every property in the city based on real estate market transactions that have occurred. A typical assessment value change for each of the assessment classes is then determined. If the homeowner's or business owner's property assessment changes by the same amount as the typical change for their assessment class, the amount they pay in property taxes will be unchanged as a result of the reassessment. If their property value change is above the typical, they will see a tax increase as a result of the reassessment and if it is below, they will see a tax decrease.

The example below assumes that The City's revenue required from property taxes stays unchanged from one year to the next based on Council's approved budget. Table 2 shows an example of reassessment impacts on property taxes using revenue neutral.

The revenue neutral system ensures that a municipality can meet its budgetary requirements each year and does not directly tie the volatility of the real estate market to the revenues collected. In this way, property owners are ensured of a fair and transparent system and that the municipality only collects what it needs each year.

Table 1. Revenue Neutral: Visual Explanation

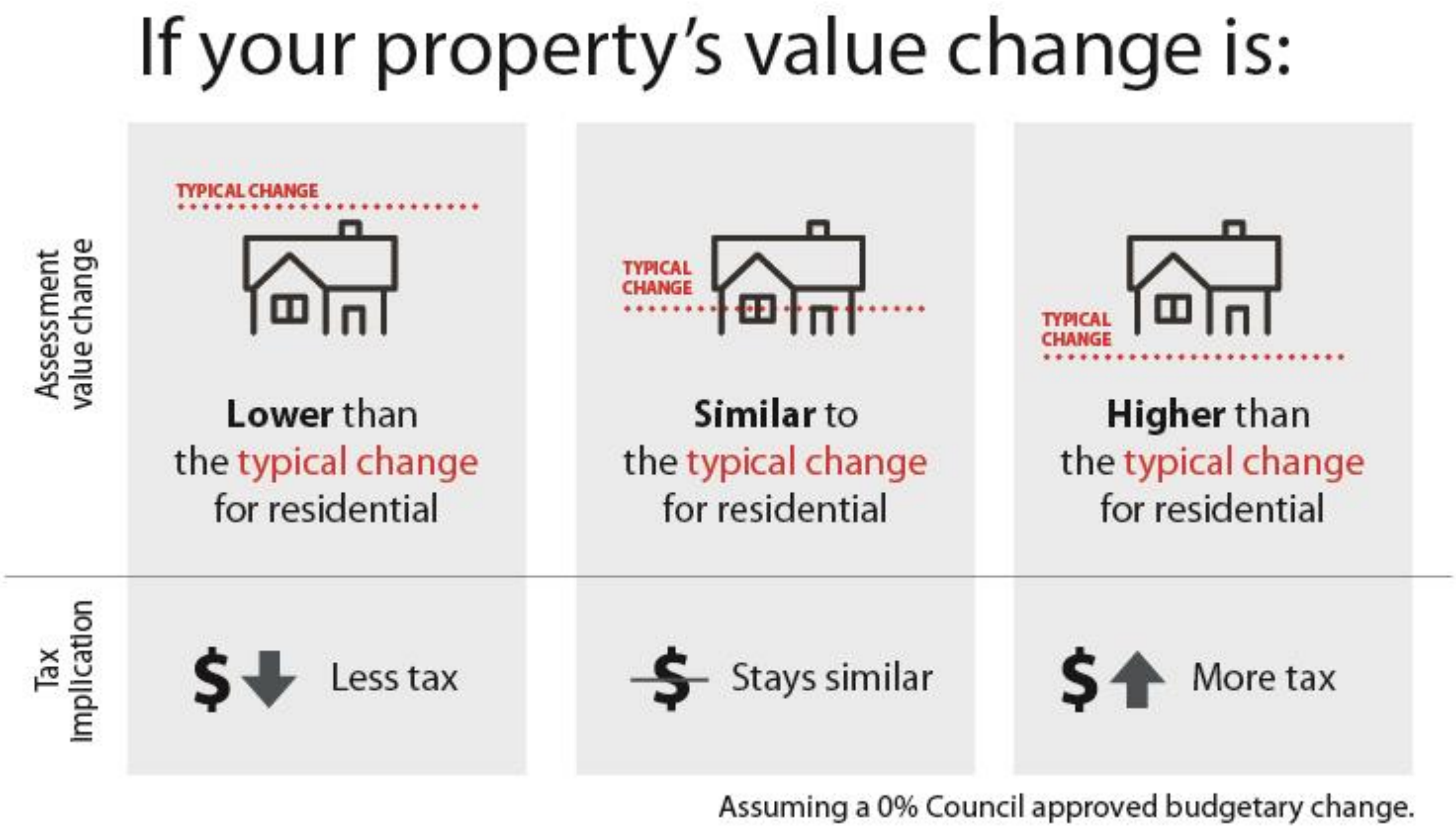

Table 2: How Revenue Neutral Works – A Typical Cycle

The figures below are hypothetical and are intended for illustration purposes.

Year 1 Tax Rate Calculation Budget ÷ Assessment Base = Tax Rate $8,000 ÷ $800,000 = 0.01	House 1	House 2	House 3	
Assessed Value x Tax Rate = Year 1 Taxes Payable	$150,000 x 0.010000 = $1,500	$250,000 x 0.010000 = $2,500	$400,000 x 0.010000 = $4,000	= $800,000 Assessment Base = $8,000 Budget Requirement
Year 2 Reassessment Assessment Change (per cent)	$165,000 +10 per cent	$275,000 +10 per cent	$440,000 +10 per cent	= $880,000 Total = +10 per cent overall increase
Year 2 Revenue Neutral Tax Calculation with No Budget Change Budget ÷ Assessment Base = Tax Rate $8,000 ÷ $880,000 = 0.009091				
Assessed Value x Tax Rate = Year 2 Taxes Payable Year over Year Tax Change (per cent)	$165,000 x 0.009091 = $1,500 0 per cent	$275,000 x 0.009091 = $2,500 0 per cent	$440,000 x 0.009091 = $4,000 0 per cent	= $880,000 Assessment Base = $8,000 Budget Requirement
Year 3 Reassessment Assessment Change (per cent)	$165,000 0 per cent	$269,500 -2 per cent	$418,000 -5 per cent	= $852,500 Total = -3.125 per cent overall increase
Year 3 Revenue Neutral Tax Calculation with No Budget Change Budget ÷ Assessment Base = Tax Rate $8,000 ÷ $852,500 = 0.009384				
Assessed Value x Tax Rate = Year 3 Taxes Payable Year over Year Tax Change (per cent)	$165,000 x 0.009384 = $1,548 +3 per cent	$269,500 x 0.009384 = $2,529 +1 per cent	$418,000 x 0.009384 = $3,922 -2 per cent	= $852,500 Assessment Base = $8,000 Budget Requirement