Tax Equity: Narrowing the gap between residential and non-residential property taxes

Issue: Non-residential properties continue to pay a greater proportion of property taxes than residential rate payers, even though it is not clear that they use a greater proportion of the benefits received from property tax revenues.

Executive Summary

Property taxes vary widely across municipalities in Alberta. This reflects differences in assessment bases as well as the latitude given to municipalities to raise revenue in different ways under the Municipal Government Act, such as different classes of property taxes, user fees, etc. Nonetheless, there is a tendency to place a greater proportion of the tax burden on businesses versus those accessed by residents. Although it is very difficult to measure and compare the public services received by businesses versus those received by residents, it seems unlikely that the cost of providing municipal services to businesses can be double, or higher, as some tax rates show. Efforts should be made to narrow the residential vs. Non-residential tax gap to a more equitable ratio that can be defended with data to justify why one class could pay more than the other.

BACKGROUND

Economic research indicates that tax rates affect people's behavior. The most important conclusion is that high taxes contribute to lower rates of economic growth, reduced rates of personal income growth, lower rates of capital formation, and reduced entrepreneurship.[1] In our regional municipalities, businesses continue to pay a disproportionate amount of taxes compared to their residential counterparts and although the gap between residential and non-residential tax rates has narrowed in recent years a formal policy should be adopted to ensure all tax payers in Medicine Hat, the Town of Redcliff and Cypress County pay a proportionate share of taxes.

One way to compare business burden to residential burden is the property tax rate ratio. This ratio is calculated by dividing the non-residential property tax rate by the residential property tax rate. For comparison purposes the average tax gap ratios by type of municipality in Alberta can be reviewed in the table below:

Market value is the price a property might be expected to sell for, if sold by a willing seller to a willing buyer, after appropriate time and exposure in an open market. There are three approaches to determine the market value assessment of a property: the sales comparison approach; the cost approach; and the income approach. One or more of these approaches is used to arrive at a property's assessed value using the market value standard.

2021 Tax Gap Ratios by Type of Municipality		
Type:	**Amount in Calculation**	**Average Tax Gap Ratio**
City	19	1.82
Specialized Municipality	6	4.06
Municipal District	63	3.48
Town	104	1.70
Village	78	1.56
Summer Village	49	1.51
Improvement District	7	1.72
Special Area	1	2.57
Total Alberta	330	**2.02**

In Medicine Hat, this ratio had slowly narrowed, falling from a ratio of 3.16 in 2008 to 2.25 in 2015, remaining largely consistent past that point, with the tax ratio still measuring 2.25 in 2021. In speaking with city administration there is no current policy in place to ensure the narrowing of the tax gap continues into the future, nor is there a policy to state what the preferred ratio may be.

[1] *Charles Lammam, Milagros Palacios, Niels Veldhuis, Submission to British Columbia's Expert Panel on Business Taxation, 2012*

[2] *City of Medicine Hat, History of Municipal Tax Rate (SF vs Non-Res)*

While completing an annual review of property tax rates across Alberta, it was revealed that out of the 18 cities, Medicine Hat placed amongst the highest in terms of the tax gap ratio. Only 3 of the 18 cities had a tax gap ratio higher than Medicine Hat with Lethbridge at 2.44, Edmonton at 2.85, and Calgary at 3.42. Jurisdictions near Medicine Hat, with the exception of the Town of Redcliff at 2.64, all ranked lower. This includes Cypress County: 2.11, Brooks: 1.42, and Town of Bow Island: 1.31. Similar sized municipalities (based upon population of 50,000 to 70,000) also had a lower tax gap ratio with Grande Prairie showing a 1.75 gap ratio and St. Albert showing a 1.36 gap ratio.

In addition, Medicine Hat sits in 233rd position, out of 309 municipalities in Alberta in relation to the non-residential municipal tax rate. Comparatively Redcliff ranks in at 245th and Cypress County comes in at the 52nd spot across Alberta. Out of the 18 cities specifically in Alberta, Medicine Hat ranks 14th; only Edmonton, Lethbridge and Wetaskiwin have a higher non-residential municipal tax rate than Medicine Hat.

The 2021 Municipal Non-Residential Tax Rates for Alberta Cities is provided below:

Municipality	Non-Residential Municipal Tax Rate	Linked tax ratio: NR divided by residential/farm land
Airdrie	10.17585	2.10
Beaumont	9.94854	1.39
Brooks	11.92186	1.42
Calgary	16.51300	3.42
Camrose	13.12600	1.48
Chestermere	7.23880	1.42
Cold Lake	12.79750	1.45
Edmonton	19.97920	2.85
Fort Saskatchewan	9.92232	1.73
Grande Prairie	17.14870	1.75
Lacombe	9.35870	1.14
Leduc	8.54100	1.12
Lethbridge	21.32740	2.44
Lloydminster	11.91850	1.80
Medicine Hat	15.28070	2.25
Red Deer	14.67340	2.02
Spruce Grove	9.44870	1.40

St. Albert	11.55768	1.36
Wetaskiwin	19.29550	2.00

Source: open.alberta.ca/opendata/municipal-financial-and-statistical-data (Current as of November 21, 2021)

Property taxes have important implications for economic competitiveness. In jurisdictions across Canada, studies have shown numerous ways in which businesses pay a disproportionate share of the tax burden. This problem is not Alberta's alone and others have tried to solve it. For example, some jurisdictions have opted to recommend a rate ratio cap, effectively preventing the ratio from getting too large.[3] Others have followed this trend, but singled out small business to benefit from a lower tax gap ratio at a quicker rate than they were able to implement for all business.[4]

ANALYSIS

In a time when economic competitiveness is not only regional, or provincial, but world-wide, we need to ensure that Medicine Hat and our region is viewed as not only competitive, but a leader when it comes to attracting new business to our area. Although we can appreciate that the tax gap has been narrowing in recent years, we must ensure that the downward trend continues and that business can be confident in the path the City is taking in regards to business taxation.

Explicitly considering policies and objectives has at least three benefits: it enhances financial transparency, accountability, and prudence. Setting out objectives in a public document enhances transparency, allowing businesses and other stakeholders to see why a municipality is seeking revenue from those sources. In enhancing transparency, it makes it easier for voters and other concerned parties to hold politicians accountable. Principle-based revenue sourcing encourages prudent decisions that will enhance equity and competitiveness. Accountability is important for businesses because they have no direct influence in municipal politics. They cannot vote, but are subject to taxation. Municipalities that engage all stakeholders in budget planning and sufficiently report on the collections and expenditures are more accountable to ratepayers (citizens and businesses alike). Enhanced accountability helps ensure ratepayer dollars are prudently spent. [5]

RECOMMENDATIONS

The Medicine Hat & District Chamber of Commerce recommends the City of Medicine Hat, the Town of Redcliff, and Cypress County:

1. Adopt a policy by the 2024 tax year to reduce the residential and non-residential property tax gap to a ratio of 2.0 or lower, which is in line with Cities across Alberta.
2. Create greater transparency in how the municipality sets its' residential and non-residential tax rates by developing a system, policy or costing method communicating and explaining to local businesses how tax rates and associated costs are set.

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[3] British Columbia, Community Charter, 2003, http://www.bclaws.ca/Recon/document/ID/freeside/03026_00

[4] City of Toronto, Enhancing Toronto's Business Climate, 2005, https://web.toronto.ca/wp-content/uploads/2017/08/947e-Enhancing-Toronto-Business-Climate.pdf

[5] Principles are drawn from: Harvey Rosen, Beverly Dahlby, Roger Smith and Paul Boothe, Public Finance in Canada, 2003; Vancouver, Tax Policy Review, 2007; and Kate Berniaz, Municipal Property Tax in BC: Principles and Provincial Strategies to Shape Local Tax Distribution Policy, 2009.