



Local Governments in the 21st Century: What are the Funding Options?

Presentation to the
Municipal Finance Authority of British Columbia
Victoria, BC
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Key Takeaways

- Municipalities in Canada are fiscally healthy but fiscal health may have been at the expense of overall health – services and infrastructure
- Local governments would benefit from a mix of taxes
- Link taxes to expenditures

Outline of Presentation

- A little bit about IMFG
- State of municipal finances
 - British Columbia
 - Comparisons with Ontario, Alberta, Quebec
 - International comparisons
- Linking taxes to expenditures
- Selected revenue options
- Final observations

Institute on Municipal Finance and Governance

IMFG | Institute on Municipal Finance and Governance

IMFG (est. 2004) is the only institute of its kind in North America, which focuses exclusively on the municipal finance and governance challenges facing cities and large city regions.

Focus

As the size and scope of responsibilities for cities expands, do local governments have the appropriate financial and governance arrangements to effectively and efficiently deliver services to residents?

Mandate

- Conduct independent research
- Spark and inform public debate
- Engage the academic and policy communities

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website: munkschool.utoronto.ca/imfg/

Recent Publications

Cities, Data, and Digital Innovation, by Mark Kleinman

Cost Overruns on Infrastructure Projects: Patterns, Causes, and Cures, by Matti Siemiatycki

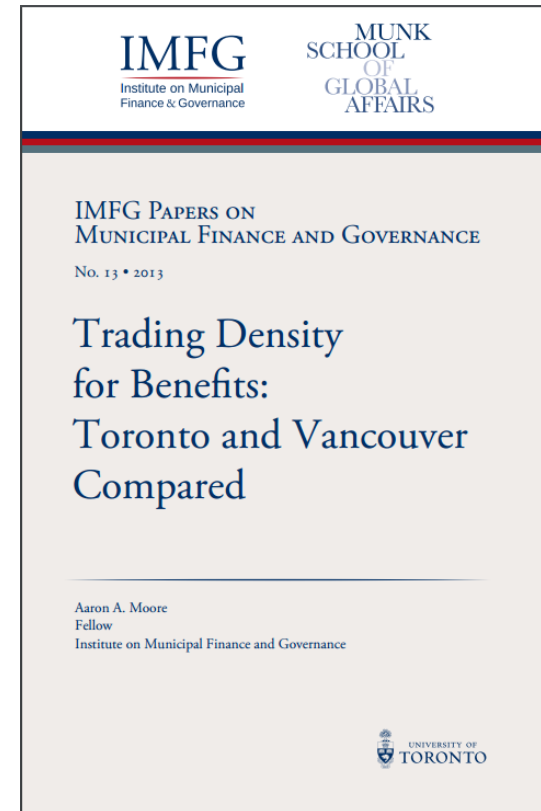
Municipal Employee Pension Plans in Canada: An Overview, by Bob Baldwin

A Good Crisis: Canadian Municipal Credit Conditions After the Lehman Brothers Bankruptcy, by Kyle Hanniman

How to Reform the Property Tax: Lessons from Around the World, by Enid Slack and Richard M. Bird

IMFG@10: The Past, Present, and Future of City Finance and Governance, by Richard M. Bird, Alan Broadbent, Enid Slack, and Zack Taylor

And more...

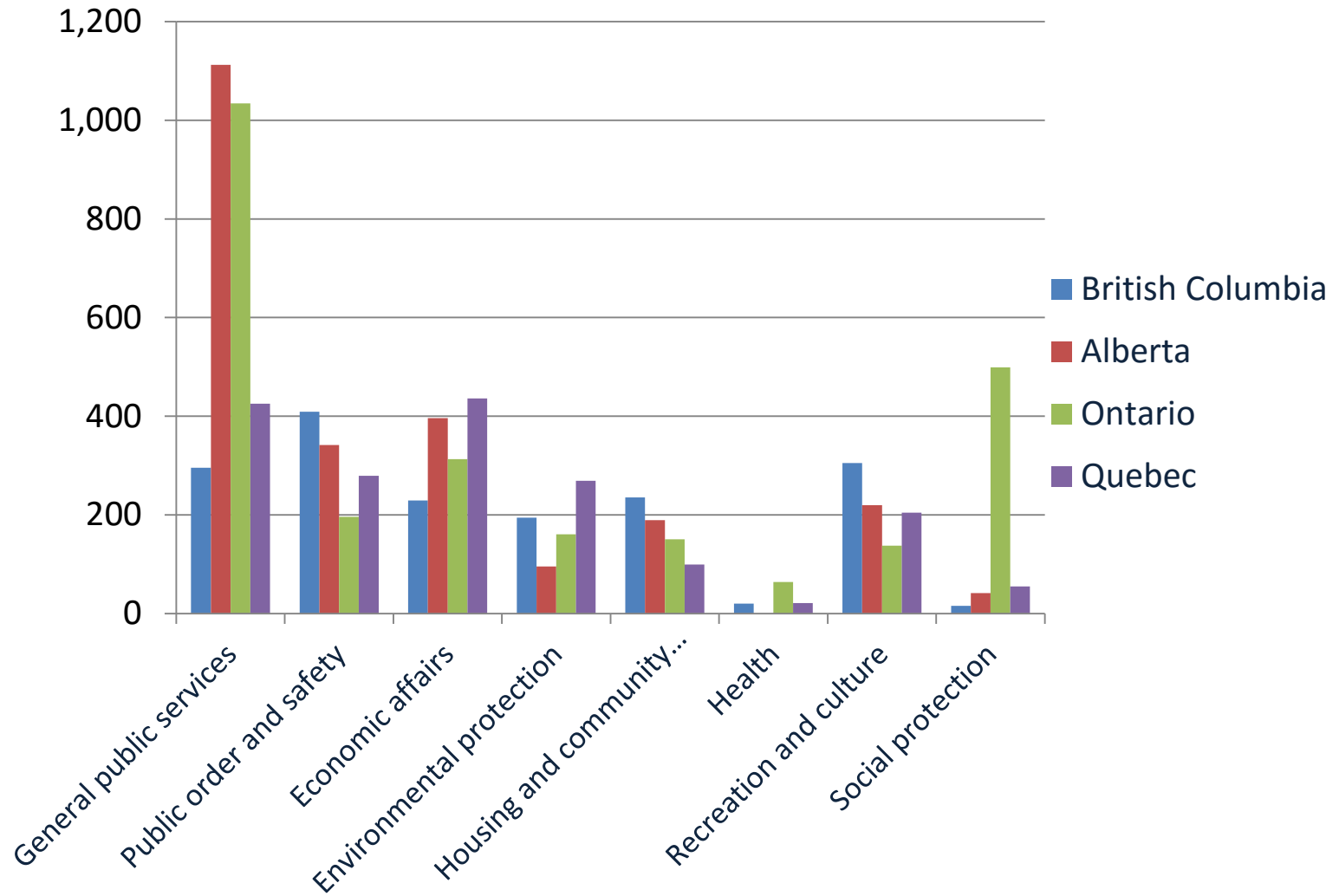


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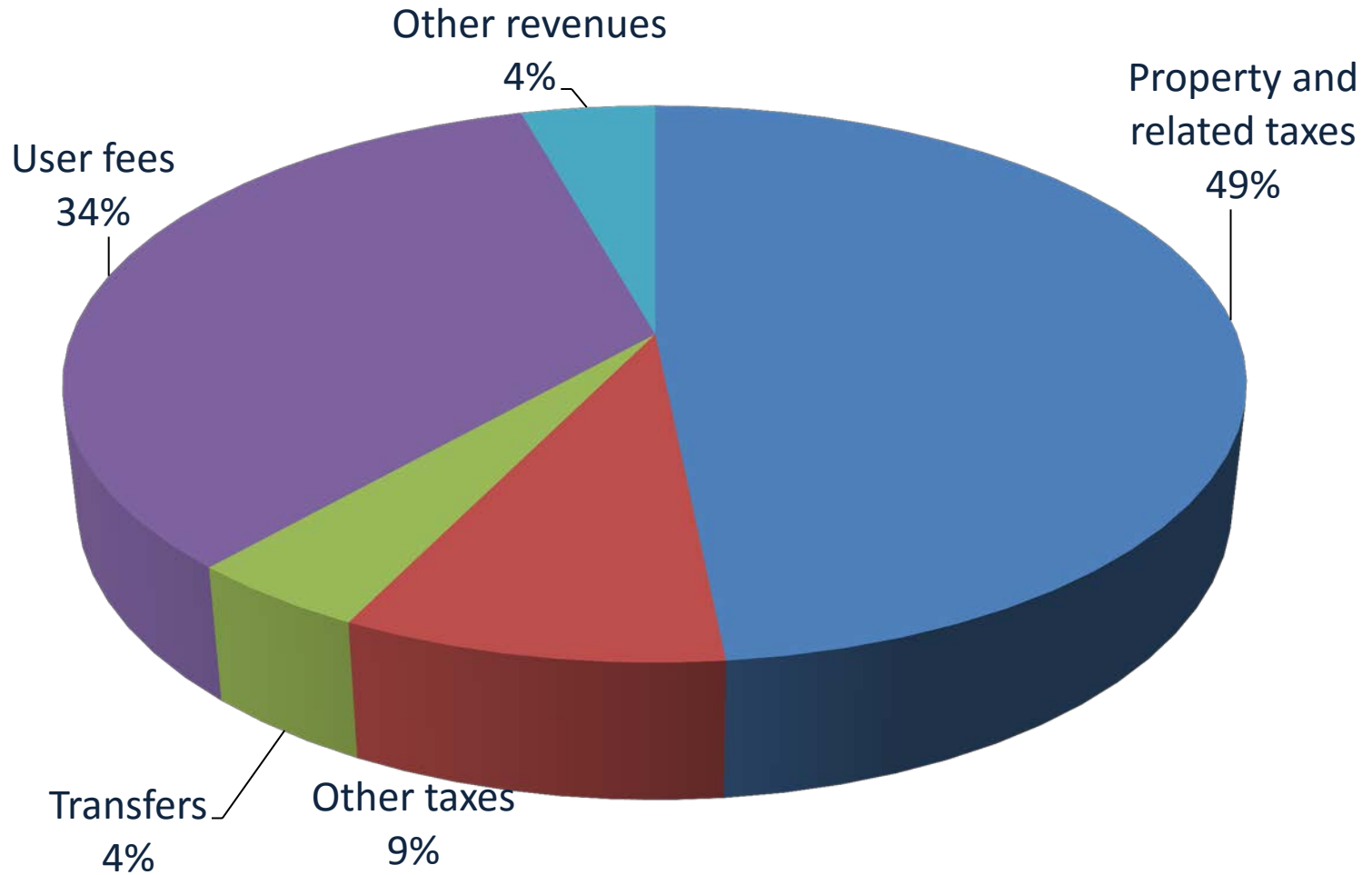
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State of Municipal Finances

Municipal Expenditures Per Capita, 2013

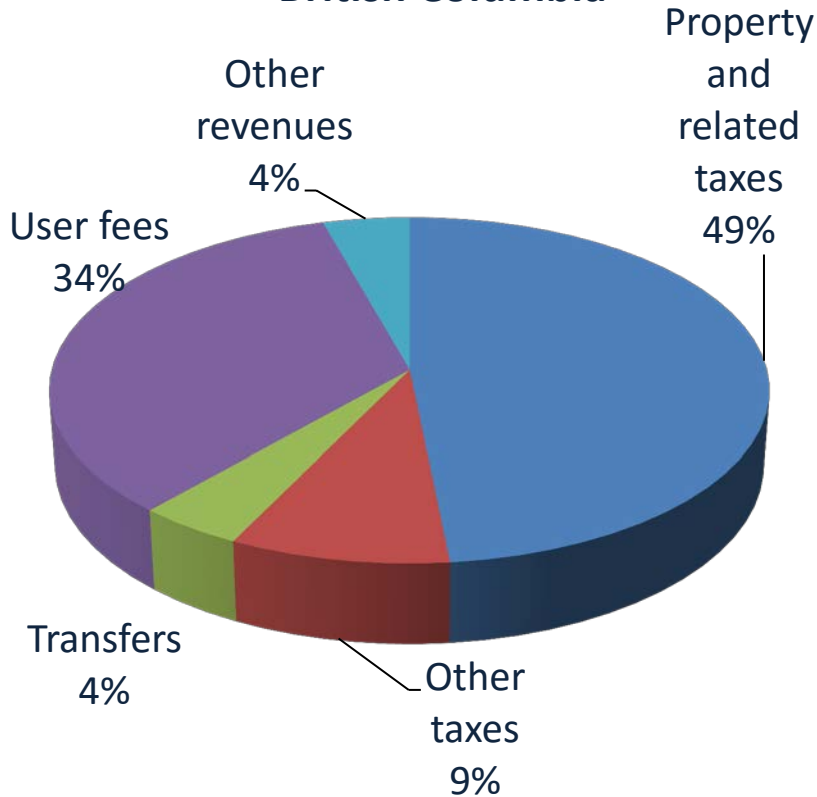


Distribution of Municipal Revenues, BC, 2013

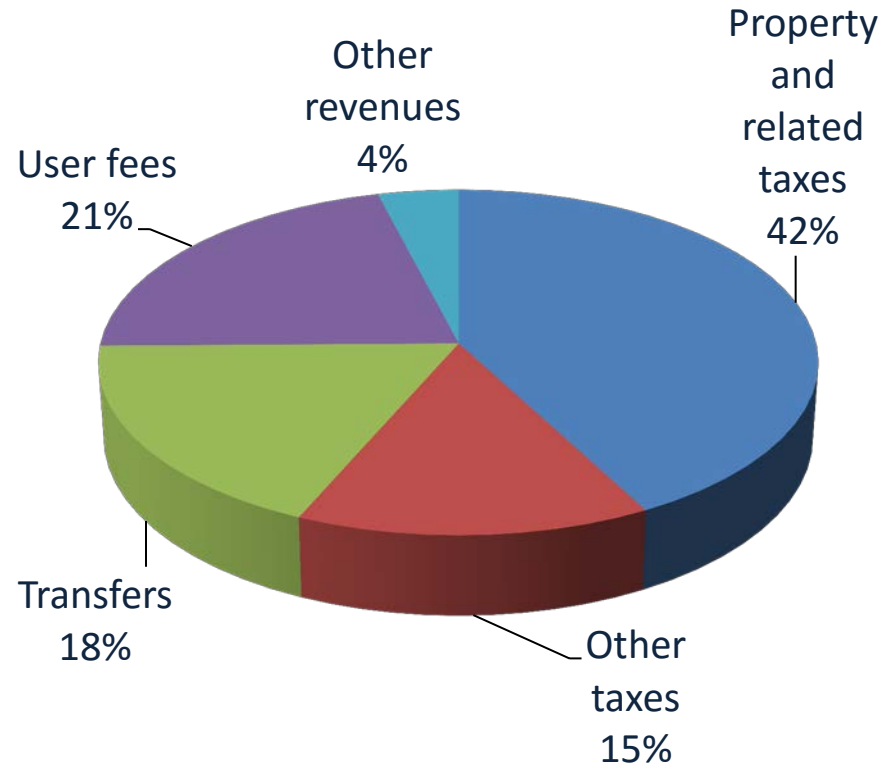


Distribution of Municipal Revenues, 2013

British Columbia

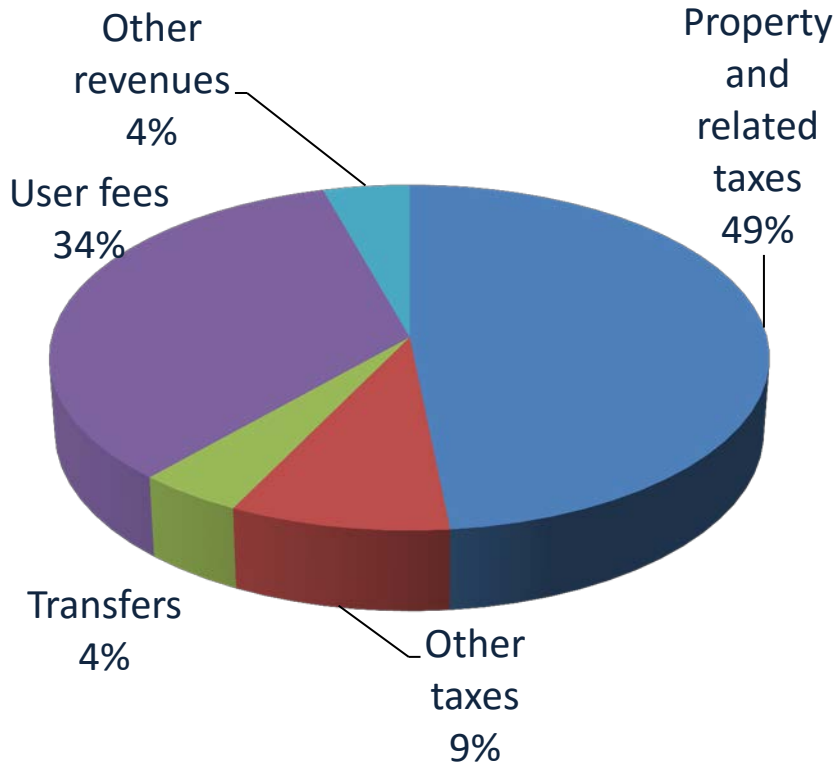


Alberta

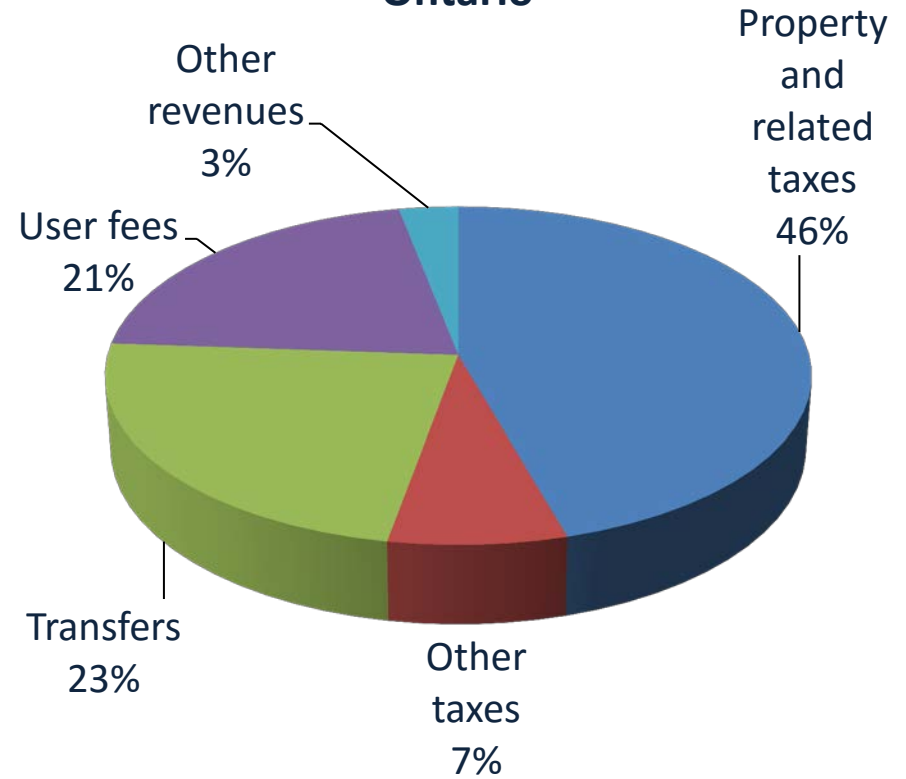


Distribution of Municipal Revenues, 2013

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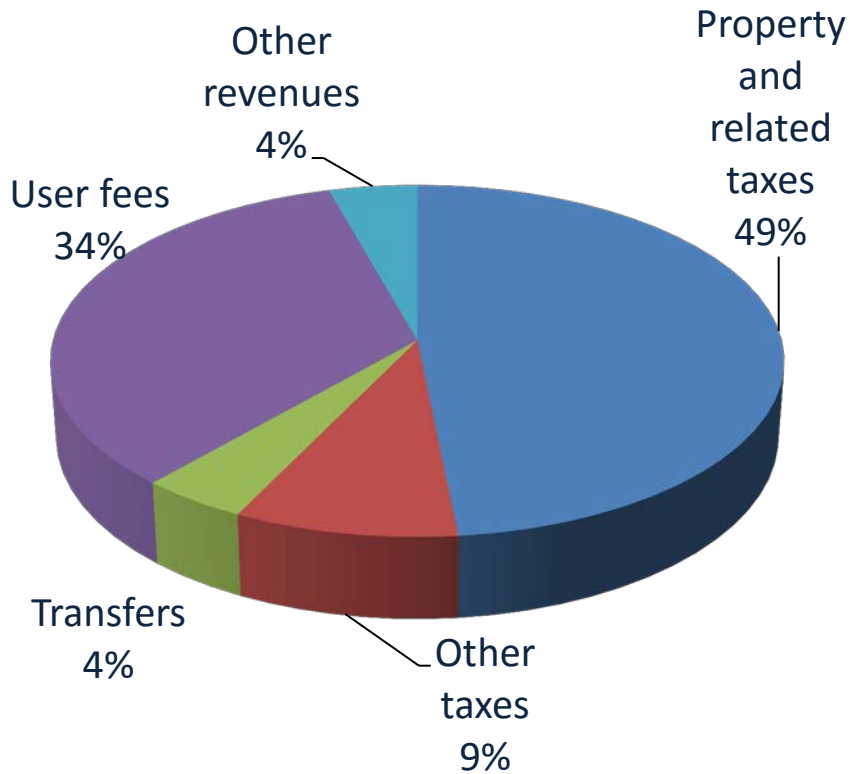


Ontario

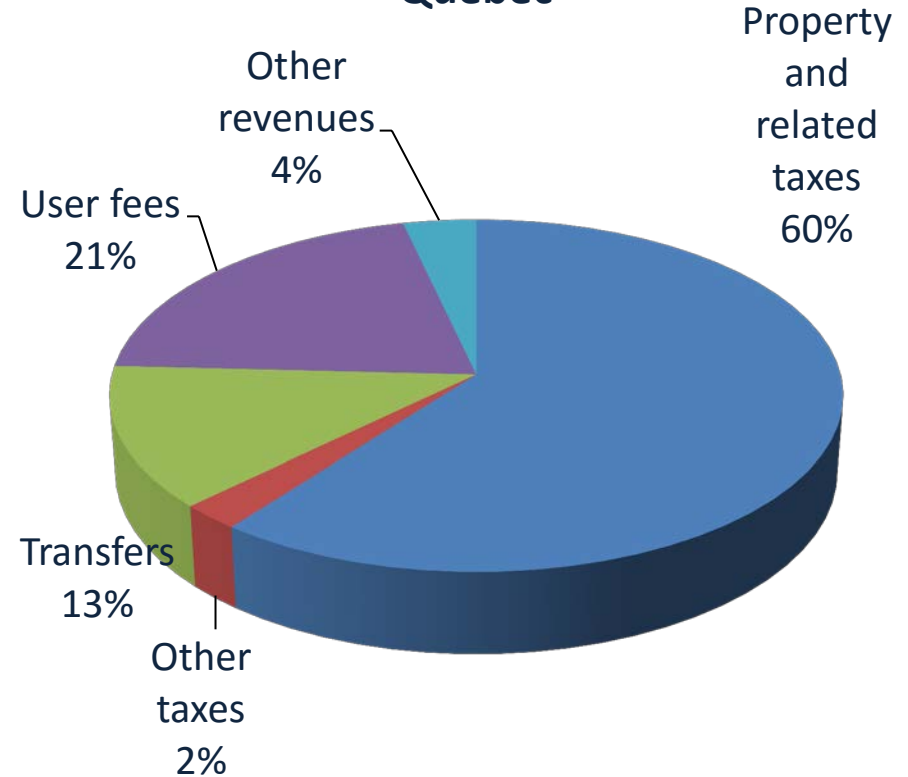


Distribution of Municipal Revenues, 2013

British Columbia



Quebec



Other Municipal Taxes in Selected Provinces

- Land transfer tax
- Amusement taxes
- Hotel taxes
- Poll tax
- Vehicle registration tax
- Billboard tax
- Revenue sharing e.g. fuel tax sharing



Fiscal Challenges Facing Municipalities

- Federal and provincial offloading
- Need to be internationally competitive
- High costs associated with sprawl
- Impact of economic downturn
- No diversification of revenue sources

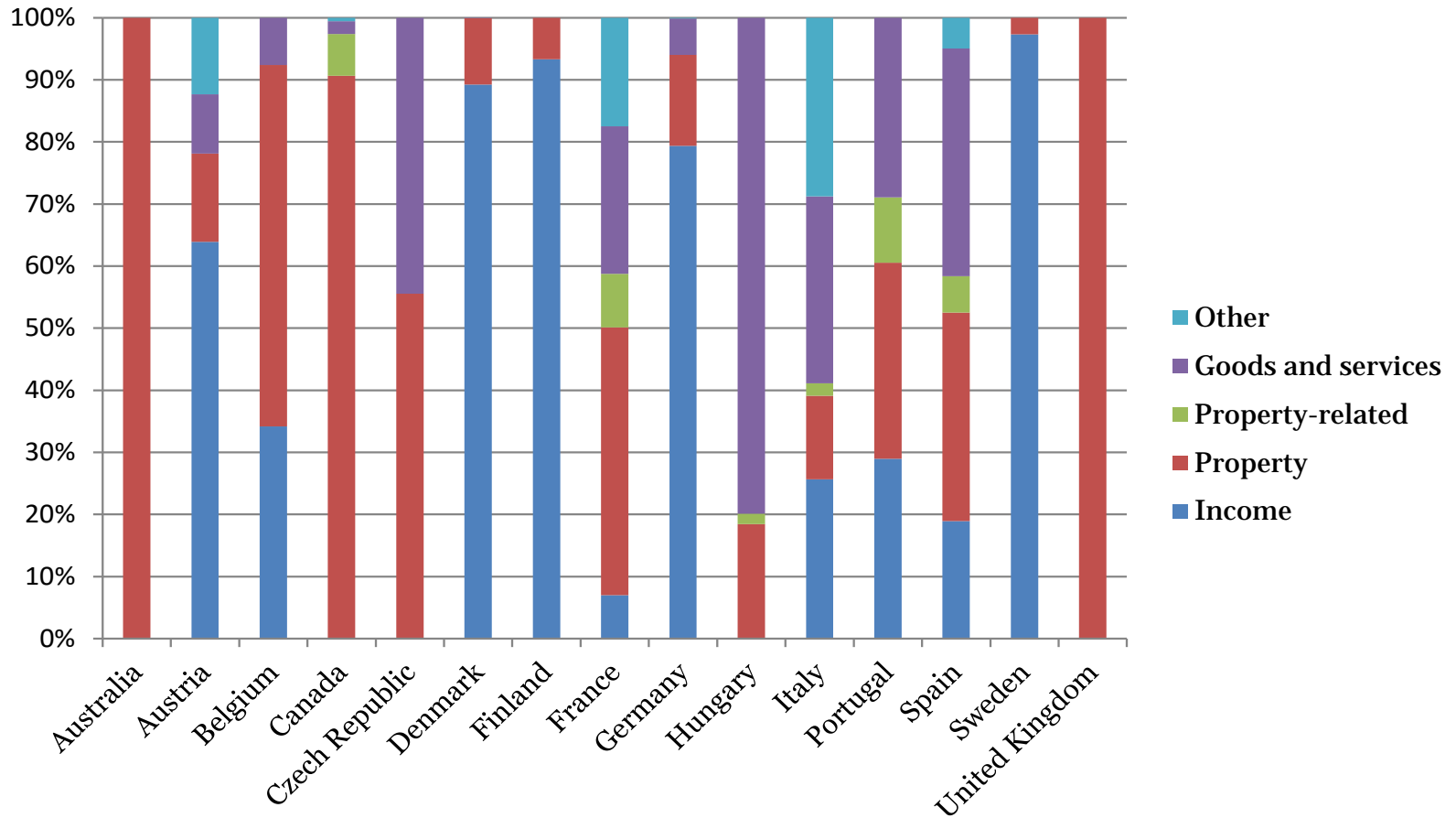
Is There a Municipal Fiscal Imbalance?

- Most municipalities in Canada have done well on fiscal measures:
 - Size of operating deficit (no fiscal imbalance)
 - Amount of borrowing for capital
 - Size of reserves
 - Rate of property tax increases
 - Reliance on provincial grants
 - Extent of tax arrears

Is There a Municipal Fiscal Imbalance?

- Fiscal health may have been achieved at the expense of municipal overall health:
 - State of municipal infrastructure
 - Quality of service delivery
- Infrastructure and services are difficult to measure
- May need to look at new revenue sources

Sources of Local Taxation, Selected OECD Countries, 2012



Source: OECD (2014) Revenue Statistics, 2011-2012.

International Experience

- More than 80% of local tax revenues from **property taxes** in Australia, New Zealand, Ireland, United Kingdom, Canada, US
- More than 80% of local tax revenues from **personal and corporate income taxes** in Sweden, Germany, Switzerland
- **Sales taxes** are levied mainly by cities in the US
- **Mix of taxes** in Spain (40% of local tax revenues from sales tax; 30% from property taxes; 20% from income tax and 10% from other)

Taxes in Major International Cities

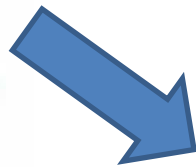
Figure 21: Taxes in Major International Cities

Taxes	Toronto	New York	Paris	London	Madrid	Berlin	Tokyo
Property / Land	x	x	x	x	x	x	x
Land Transfer*	x	x	x			x	x
Billboard	x						
Sales / Value Added*		x			x	x	x
Personal Income*		x			x	x	x
Business Income		x	x		x	x	x
Vehicle		x			x	x	x
Other taxes		18	5		3	16	12

*In some instances, shared with senior orders of government.

Linking Taxes to Expenditures

Linking Taxes and Expenditures



Linking Taxes to Expenditures

- People want to see what they are getting for their taxes
- Linking taxes and services increases public support
- Examples of ballot initiatives in the US to pay for transit
- Public sector operates more efficiently when there is a link between expenditure and tax decisions – the Wicksellian connection

Different Services – Different Revenue Tools

Private

Water
Sewers
Garbage
Transit

Public

Police
Fire
Local parks
Street lights

Redistributive

Social assistance
Social housing

Spillovers

Roads/transit
Culture
Social assistance



User fees



Property tax
Sales tax



Income tax



**Intergovernmental
transfers**

Different Infrastructure – Different Fiscal Tools

Taxes



short asset life
(police cars,
computers)

User fees



identifiable beneficiaries
(transit, water)

Borrowing



large scale assets
with long life
(roads, bridges)

Different Infrastructure – Different Fiscal Tools

Development charges

P3s

**Land value capture
taxes**



growth-related costs;
new development or
redevelopment
(water, roads, sewers)



large in scale;
revenue stream;
measurable results
(toll roads)



increase property values
(transit)

A Mix of Taxes

- Local governments benefit from a mix of taxes:
 - Range of expenditure responsibilities
 - Services used by commuters/visitors
 - Revenues that grow with the economy (elastic)
 - Tax distortions may offset each other
 - Increase municipal flexibility in adapting to local circumstances
- Ability to set tax rates: more responsible and more accountable to taxpayers

Revenue Options

User Fees -- Pricing Services Correctly

- How we pay for services affects our behaviour (e.g. how much water we consume, how much waste we generate)
- Pricing also affects nature, location and density of development
- Local governments need to price services and infrastructure correctly – manage demand for services and infrastructure



Property Tax – A Good Tax?

- Property is immovable
- Adequate, stable, predictable yield
- Visible/accountable
- Fair - related to benefits received; regressive?
- Residential rates not exported to other jurisdictions
- Minimum inter-municipal competition

But:

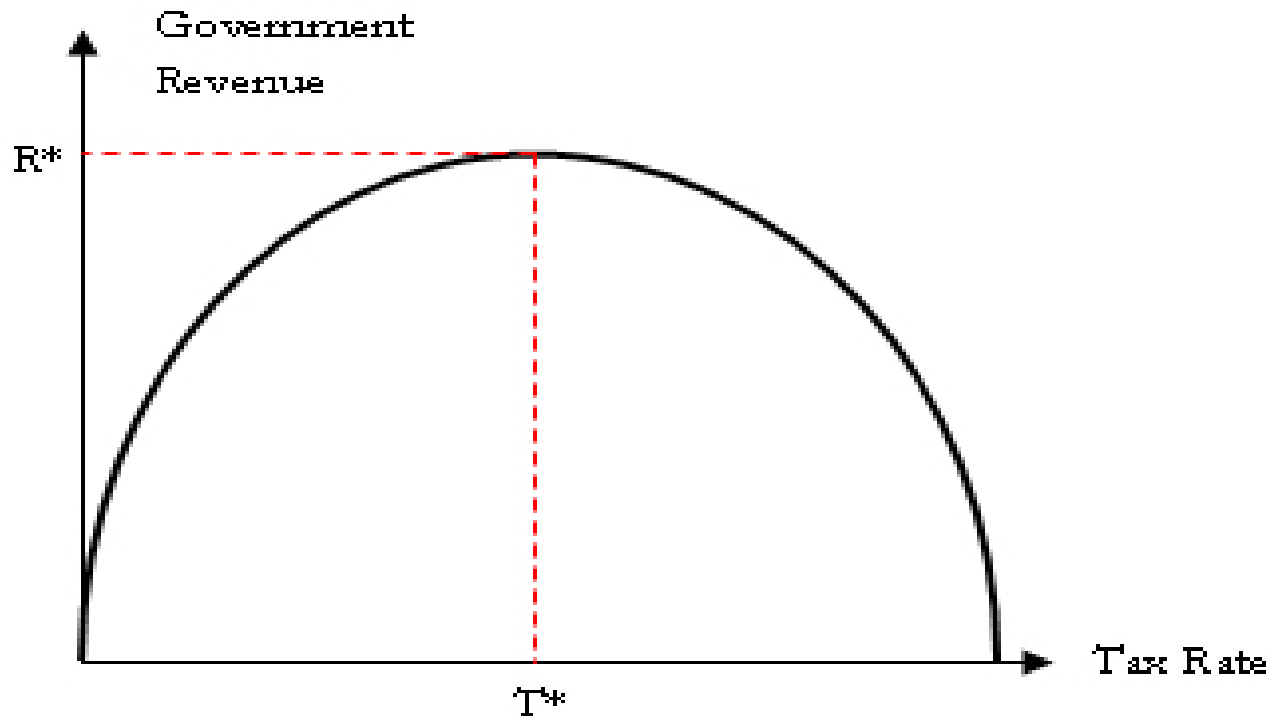
- Costly to administer -- arbitrariness of tax base
- Volatile for individual taxpayers
- Inelastic – doesn't automatically grow with economy; changing nature of business

Property Tax – Is It Enough?

- Property tax (2010) yielded 3% or more of GDP in only three OECD countries: Canada, UK, US
- More than 2% of GDP in only four OECD countries: France, Israel, Japan, New Zealand
- Less than 1% of GDP in 22 countries

How to Reform the Property Tax: Lessons from Around the World --
Enid Slack and Richard Bird, IMFG Paper No. 21, 2015

Can Property Taxes be Increased?



Revenue Hills in Toronto Area Municipalities

- Peak of the revenue hill has not been reached for residential property taxes in most municipalities (some exceptions, e.g. Oshawa)
- Closer to the peak of the revenue hill for non-residential property taxes in some municipalities but some municipalities shifting burden away from non-residential (e.g. Toronto)

Can GTA Municipalities Raise Property Taxes? An Analysis of Tax Competition and Revenue Hills – Almos Tassonyi, Richard Bird, and Enid Slack and Richard Bird, IMFG Paper No. 20, 2015

Personal Income Tax

- Elastic revenue source
- Taxes commuters if levied on the basis of origin (place of employment)
- Equitable based on ability to pay and benefits received
- Administrative costs low if piggyback onto existing system

But:

- Competition with federal and provincial governments
- Potential for inter-municipal tax competition
- May increase need for equalization

General Sales Tax

- Visible on each transaction
- Elastic revenue source
- Taxes benefits enjoyed by commuters and visitors
- Competition with federal and provincial governments
- Potential for inter-municipal competition if rates set locally

Excise Taxes

- Examples: hotel occupancy, fuel, vehicle registration, parking
- Some are benefit-related
 - e.g. vehicle registration tax is related to road use and external effects such as pollution and congestion
- Can affect consumer behaviour
 - e.g. vehicle taxes reduce automobile purchases; parking taxes reduce congestion

Federal and Provincial Transfers

- Transfers are important (for equalization and spillovers) but:
 - break the link between those who benefit and those who pay
 - not stable and predictable funding (depends on resources available)
 - no incentive to use proper pricing
 - distort local decision-making
 - accountability problems with conditional transfers when two or more levels of government fund the same service

Land Value Capture Taxes

- Recoup some or all of the unearned increment in private land values arising from public investment (e.g. roads, transit, parks) or change in regulations (e.g. zoning changes)
- Examples:
 - Betterment levies or special assessments
 - Tax increment financing
 - Sale of building rights (e.g. community amenity contributions)

Development Levies

- Covers growth-related capital cost associated with new development
- Off-site infrastructure (e.g. highways, sewer lines, etc.)
- Growth pays for itself
- Impact on land use



Final Observations

Final Observations

- Link taxes to expenditures
- User fees should fund services where beneficiaries can be identified e.g. water, sewers, waste collection, transit, roads
- Local taxes – and possibly a range of taxes – should fund services that provide collective benefits to the local community
- Intergovernmental transfers should be used for equalization, spillovers