

---

# Municipal Fiscal Imbalance Across Canada

---

Enid Slack  
Institute on Municipal Finance and Governance  
Munk Centre for International Studies  
University of Toronto

Association of Manitoba Municipalities 8<sup>th</sup> Annual Convention  
Winnipeg  
November 30, 2006

---

# Introduction

- Debate over fiscal imbalance in Canada has mainly focused on federal-provincial/territorial imbalance
- There has not been much discussion until recently about municipal fiscal imbalance (FCM report)

---

# Outline of Presentation

- Is there a municipal fiscal imbalance?
- What is different about the municipal debate compared to the federal-provincial debate?
- What can municipalities do to reduce the fiscal imbalance?
- What else needs to be done?

---

# Is There a Municipal Fiscal Imbalance?

- ❑ Do municipalities have sufficient revenue-raising capacity to meet their expenditure needs?
- ❑ Can municipalities raise existing revenues (e.g. property taxes and user fees) to meet expenditure requirements?
- ❑ Let's look at recent trends in municipal expenditures and revenues; the fiscal challenges facing municipalities; and how well they have fared

# Municipal Expenditures, 2004

|                                       | Canada | Manitoba |
|---------------------------------------|--------|----------|
| Transportation                        | 20%    | 25%      |
| Fire and police protection            | 17%    | 20%      |
| Water, sewers, garbage                | 16%    | 17%      |
| Health/social services/social housing | 16%    | 3%       |
| Recreation and culture                | 13%    | 11%      |
| General government                    | 10%    | 15%      |
| Debt charges                          | 4%     | 5%       |
| Planning and development              | 2%     | 1%       |
| Other                                 | 2%     | 3%       |

# Municipal Revenues, 2004

|                   | Canada | Manitoba |
|-------------------|--------|----------|
| Property Taxes    | 53%    | 43%      |
| User Fees         | 22%    | 24%      |
| Provincial Grants | 15%    | 21%      |
| Federal Grants    | 1%     | 1%       |
| Investment Income | 5%     | 7%       |
| Other Revenues    | 4%     | 4%       |

---

# Trends in Municipal Finance in Canada

- Over the period from 1988 to 2004, municipal expenditures in Canada increased steadily but their revenue-raising tools have not changed
- Municipal expenditures (per capita constant \$) increased by 0.9 percent per year, on average
- Municipal revenues (per capita constant \$) increased by 0.7% per year, on average

---

# Trends in Municipal Expenditures

- Which expenditures have increased as % of total expenditures?
  - Protection (fire and police), recreation and culture, environmental (water, sewers, garbage)
  
- Which expenditures have decreased as % of total expenditures?
  - Transportation, general administration, planning, debt charges

---

# Trends in Municipal Revenues

- Which revenues have increased as % of total revenues?
  - Property taxes increased from 49% of revenues in 1988 to 53% in 2004
  - User fees rose from 20% to 23%
  
- Which revenues have decreased as % of total revenues?
  - Intergovernmental transfers fell from 23% to 16%; mainly decline in provincial with some increase in federal transfers

---

# Fiscal Challenges Facing Large Municipalities

- Offloading of services
- Need to be internationally competitive
- Higher costs associated with urban sprawl
- No diversification of revenue sources

---

# Fiscal Challenges Facing Small, Rural, Remote Municipalities

- Offloading
- High per capita expenditures because of distances, inability to achieve economies of scale
- Small tax base restricts ability to raise revenues
- High cost of services means user fees can only cover a small portion of the cost

---

# Is There a Fiscal Imbalance?

- Municipalities have done well on fiscal measures:
  - ❑ Size of the 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 Fiscal Imbalance?

- *Fiscal* health may be achieved at the expense of the *overall* health of Canadian municipalities:
  - The state of municipal infrastructure (water, sewers, roads, recreational facilities, etc.)
  - The quality of service delivery (e.g. performance measures)
  - Infrastructure and services are difficult to measure

---

# Is There a Municipal Fiscal Imbalance?

- Estimates of infrastructure deficit: \$60 to \$125 billion
- Problems with studies:
  - some cover all municipal infrastructure; others cover only specific types of infrastructure
  - some separate replacement and rehabilitation from investment needs while others do not
  - data from surveys reflect vested interest in overstating the infrastructure deficit
  - most assume no policy changes in the future (e.g. efficient user fees that will result in curbing demand).
- Nevertheless, there is an emerging consensus that there is a substantial infrastructure deficit in Canada's cities

---

# Is There A Municipal Fiscal Imbalance?

- ❑ Canadian municipalities do not suffer from a fiscal imbalance because they have to balance their budgets by law and they are restricted in terms of how much they can borrow for capital
- ❑ Fiscal balance may have been achieved at expense of infrastructure and services

---

# The Federal-Provincial Fiscal Imbalance Debate

- Provinces argue that the federal government has more fiscal capacity than it needs to meet its expenditure requirements; provincial governments have less fiscal capacity than they need to meet their expenditure requirements
- It is going to get worse because of rising health care costs

---

# The Fiscal Imbalance Debate

- Federal government argues that provincial governments have access to the same tax bases as federal government (mainly income and sales taxes); why not raise taxes?
- Can the provinces raise their taxes?
- Provinces argue that they are at the limit
- Fortunately, we don't have to answer that question today

---

# What is Different about the Debate at the Municipal Level?

- Municipalities are different than federal and provincial governments:
  - Municipalities are constrained by provincial governments in terms of the expenditures they are required to make and the revenues they can raise; less flexibility on expenditure and tax decisions
  - Municipalities rely largely on property taxes to meet expenditure requirements; do not have access to income and sales taxes

---

# What is Different about the Debate at the Municipal Level?

- Unique characteristics of property tax:
  - Inelastic tax
  - Growth may be limited in the future by aging population (drop in housing starts), downsizing and limited growth in housing prices (Conference Board)
  - Ability to increase non-residential taxes limited because of over-taxation relative to services
  - Visibility restricts increases (revenue neutrality)

---

# What Can Municipalities Do?

- Can municipalities increase their own revenues?
  - ❑ There may be more room in residential property tax in some municipalities but not in non-residential property tax
  - ❑ Correct pricing would reduce demand for services and infrastructure: water, transit, garbage etc.
  - ❑ Municipalities could borrow more: borrowing makes sense for infrastructure
  - ❑ Measures still likely to fall short of what is needed

---

# What Else Can be Done?

- Upload expenditures and/or
- Download revenue-raising tools to municipalities

---

# Concluding Comments

- There is probably a fiscal imbalance at the municipal level but it is difficult to measure
- The debate at the local level is different at the federal/provincial level
- Municipalities could probably raise revenues more
- But it will still not be enough – need to upload expenditures or download revenue tools