CUPE.ca Facts&Implications

NEW REVENUE SOURCES

May 2007

New revenue sources for municipalities

The Canadian Union of Public Employees has advocated strongly for the federal government to increase its funding to municipalities for many years. The evidence shows that local governments have suffered the most from any "fiscal imbalance".

- In CUPE's federal budget submissions, we've called for increased long-term funding to eliminate the municipal infrastructure deficit, access for municipalities to a permanent and growing source of revenues as well as additional funding to municipalities for priority areas such as child care, affordable housing, water, environment, public transit, and community and social services.

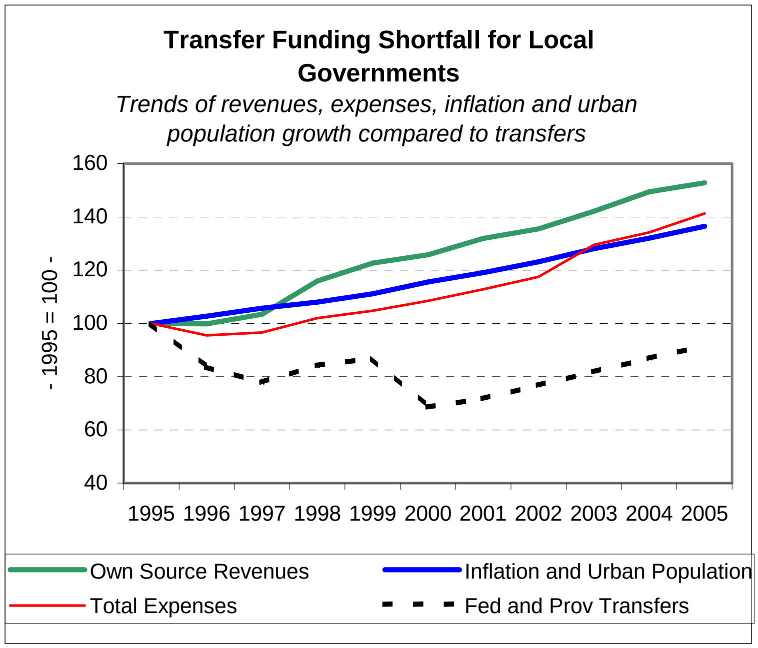
- We've argued that there is little evidence of a fiscal imbalance between federal and provincial governments, but a significant fiscal imbalance between upper levels of government and municipalities.

CUPE strongly supports the push by the *FCM* and the *Big City Mayors' Caucus* to access new revenue sources. Whatever revenue source is chosen, it is important that it doesn't lead to tax competition through local rate setting.

The Municipal Fiscal Imbalance

The federal government drastically cut transfers to provinces and to local governments in the mid-1990s. Provinces in turn severely cut transfers to local governments.

Federal and provincial governments are now in very good financial health. The federal government has accumulated over $88 billion in surpluses in the past decade while all provinces have recently registered surpluses. Federal and provincial levels of government have also significantly cut income and other tax rates.



Despite this, transfers from upper levels of governments to municipalities dropped from 26% of total local general government revenues in 1995 to only 17% of local government revenues in 2005. These transfers are still below what they were in actual dollar terms in 1995.

All measures show that, to regain ground lost since 1995, local governments should have received about $5 billion more in transfers from higher levels of government. As the attached chart shows, expenses, own source revenues, population and inflation for local governments have all increased much faster than the transfers they receive. This amounted to a funding shortfall of about $5 billion a year for 2005.

- If transfers from federal and provincial governments had kept pace with the increase of local government own source revenues, local governments would have $6.5 billion more in revenues in 2005.
- If these transfers had kept pace with local government expenses, they would have been $5.2 billion higher.
- If the transfers had kept pace with inflation and urban population growth, they would have been $4.8 billion higher.

Responsibilities continue to increase

The demands on municipalities continue to escalate, with urban regions growing, increased public demands for services, expanded unfunded mandates, and downloading and cuts by upper levels of governments.

In particular, responsibilities have increased for emergency preparedness, public safety, social housing and related social services. The highly unbalanced nature of Canada's economic growth is also causing increasing costs for local governments. On one side, municipalities in booming regions, such as Fort McMurray, are struggling with bursting demands for all types of services. On the other side, job losses manufacturing and forestry are putting greater pressure on social and community services in many towns.

Climate change will also lead to increased costs. These include costs related to *adapting* to inevitable levels of climate change, as well as costs associated with *mitigation*, reducing emissions and preventing further climate change. Some of these will include:

- Water, sewage and storm water expansion; flood and tidal surge protection
- Greater wear and tear on roads, bridges, buildings, and built systems
- Increased demand on social services, health, recreational and other human systems to deal with heat waves and other extreme climate events
- Increased risks of pests, diseases and forest fires for many communities
- Costs related to planning, assessment of risks, insurance, and "no-regrets" improvements beyond code
- Wide range of costs to reduce greenhouse gas emissions, including retrofits and fuel efficiency measures, expansion of public transit and alternative transportation, etc.

Existing revenue sources are regressive and insufficient

Local governments in other counties have access to a much wider range of revenue and tax sources that Canadian municipalities do. Property-based taxes and user fees now account for 75% of total local government revenues in Canada, up from 66% in 1995. Municipalities are dependent on property-based taxes and user fees for over 90% of their own-source revenues.

These revenue sources have many problems:

- They are highly regressive and not related to ability to pay: the property tax burden as a share of income is, on average, 3 to 5 times higher on lower income households than on higher income households.
- Property taxes are not related to many of the growing responsibilities that municipalities are increasingly obliged to provide.
- User fees exclude many citizens and residents from accessing services.
- Property tax assessment systems have been beset by a number of problems.
- Their revenues are inelastic and don't grow automatically with the economy.
- Property taxes perversely encourage urban sprawl, leading to much greater costs of providing services in future years and greater environmental damages.

The gas tax transfer provided through the *New Deal for Cities and Communities* was a positive step, but it is woefully insufficient to address current and future needs. When fully phased in, this transfer will provide $2 billion a year, which is barely enough to reduce the infrastructure gap and much less eliminate it within a generation. The total infrastructure gap is now estimated at over $100 billion and growing by at least $2 billion a year.

The 2007/8 federal Budget enshrined the $2 billion transfer to 2013-14, without escalating it to inflation or population increases. With Canada's urban population growth increasing at about 1% a year and inflation rising at 2%, this means that the real per person value of the transfer will lose about 3% of its per capita value each year. With compounding, the transfer will lose 23% of its value in seven years.

Privatization and P3s are not the solution

The federal government did not only provide a transfer that is inadequate and deteriorating in value, but it is forcing additional costs on municipalities as a condition of receiving federal infrastructure funding. The 2007 Budget announced that proponents seeking major project funding from the $10.9 billion *Building Canada Fund* and the gateways and border crossings fund would have to demonstrate that they had "fully considered" public private partnerships.

By creating a new fund for P3 projects, the Conservative government is showing that it wants to promote P3s and privatization, even though these will cost municipalities and residents more in both the short term and the long term. Off-book P3 financing for infrastructure projects can appear attractive in the short term, but it almost always leads to higher costs over the longer term, loss of control, less accountability, poorer services, and greater risks for the municipality.

Municipalities need access to increased long-term, predictable and growing revenue sources. They shouldn't be pushed into participating in expensive P3 schemes that involve high private sector borrowing costs and loss of public control and accountability.

Considerations for new revenue sources

CUPE supports the *FCM* and the *Big City Mayors' Caucus* push for access to new revenue sources.

Sharing the equivalent of one cent of the GST with municipalities appears to be a logical solution: the GST is a relatively stable source of revenues that grows in line with the economy. The approximately $5 billion in annual revenues raised by one cent of the GST is roughly equivalent to the annual shortfall that municipalities have suffered from lower transfers.

Whatever revenue source is chosen, it is important that it doesn't lead to tax competition through local rate setting. This could lead to unproductive tax avoidance, more complicated and expensive administration, and increased levels of inequality.

sl/cope491
S:\Research\WPTEXT\FCM 2007\English\New revenues needed for municipalities.doc
May 28, 2007