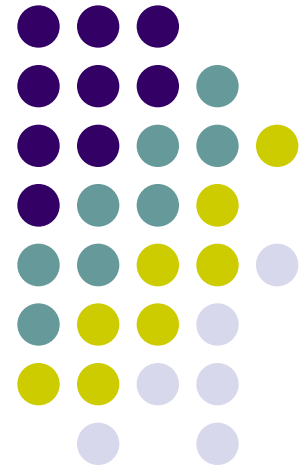


PAYING FOR LOCAL GOVERNMENT SERVICES IN LARGE METROPOLITAN AREAS

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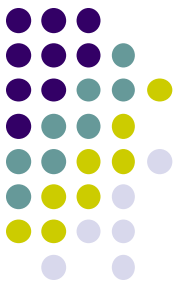


OUTLINE OF PRESENTATION



- How are large cities and metropolitan areas different than other cities?
- How do you pay for services?
- How do you pay for infrastructure?
- Are large cities treated differently in practice?

Demographic and Economic Differences



- Demographic:
 - Larger population
 - Higher population density
 - More heterogeneous population
- Economic:
 - Generate employment, wealth, and productivity growth
 - Key to the economic success of the country





Expenditure Differences

- Expenditures per capita are higher in large cities and metropolitan areas:
 - London: operating expenditures 48% above the average for all local governments in the country
 - Toronto: expenditures per household 44% higher than municipalities in the surrounding region



Expenditure Differences



- Large cities provide more services than governments in smaller urban and rural areas
- Large cities not only have to provide transportation and communications infrastructure to attract businesses, they have to provide services to attract and retain highly trained human capital



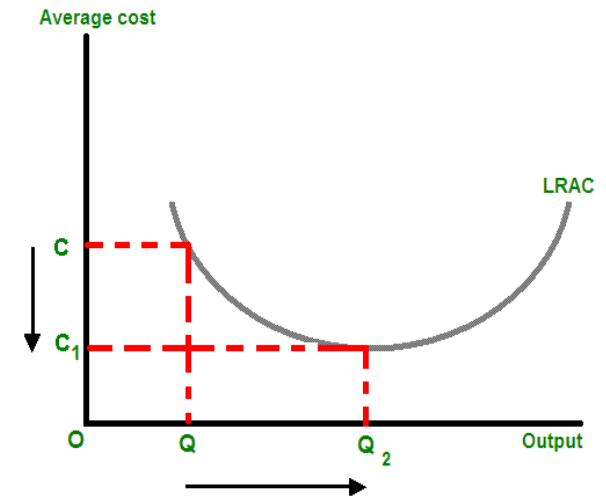
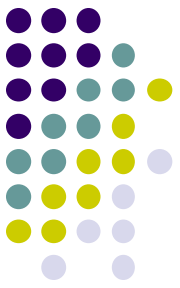
Expenditure Differences



- High concentration of special needs -- higher expenditures on social services, social housing, and public health
- Higher concentration of people -- more specialized police services
- Higher densities -- more specialized training and equipment for fire fighters
- Public transit system only in large cities because of the density required
- Major cultural facilities only in large cities because they require a minimum size

Economies of Scale?

- Spreading fixed costs over a larger population lowers per capita costs (e.g. public transit)
- Economies from bulk purchases (e.g. busses, computer equipment, etc.)
- Lower overhead costs from municipal amalgamation



Economies of Scale?



- Empirical evidence shows economies of scale are very service-specific
- Some economies of scale in central administrative functions; services with large capital inputs e.g. transportation, water and sewage systems
- Difficult to draw municipal boundaries based on economies of scale
- Cities can also become too large – diseconomies of scale

Revenue Raising Differences



- Greater ability to raise revenues:
 - Property tax – higher property values; more commercial and industrial properties
 - Income taxes – higher level of economic activity
 - Sales taxes – higher level of economic activity; tax generates significant revenues from commuters and visitors
- Factors less mobile in large geographic area



How Should Large Cities be Financed?



- Large cities should have greater fiscal autonomy than other urban or rural areas –
 - greater responsibility for local services
 - greater ability to levy own taxes and collect own revenues
 - less dependence on intergovernmental transfers



Benefit Model

- Role of local government to provide goods and services
- Those who pay fees or taxes to finance local government expenditures should also be those who benefit from those expenditures
- Application of benefit model depends on nature of services

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



What is a “Local” Tax?

- A local tax is one where the local government:
 - determines whether the tax is imposed
 - determines the tax base
 - sets the tax rate**
 - collects the revenue and enforces the tax
 - receives the revenue



What is a “Good” Local Tax?

- Immobile tax base
- Adequate, stable and predictable tax yield
- Difficult to export
- Visible and accountable
- Fair
- Minimize harmful inter-municipal competition
- Easy to administer and collect

Not all criteria can be met at the same time

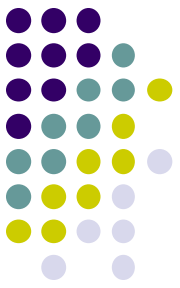
Property Tax



- Good tax for cities:
 - Immobile
 - Visible
 - Accountable
- But ...
 - restricts revenue flexibility -- no country is able to raise more than 10% of total tax revenues from the property tax
 - metropolitan areas need more than the property tax to deliver a wide range of services

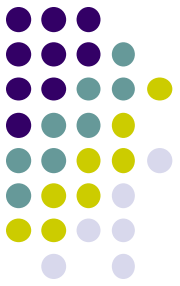
Personal Income Tax

- Elastic
- Potential to tax commuters
- Ability to pay and benefits received
- Administrative costs low if piggyback onto existing system
- Competition with central government; potential for inter-municipal tax competition
- May create need for equalization

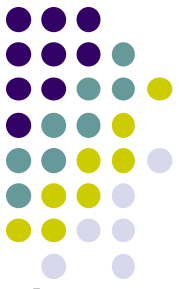


General Sales Tax

- Visible on each transaction
- Elastic
- Taxes benefits enjoyed by commuters and visitors
- Low administrative costs if piggybacked
- Regressive
- Competition with central government
- Potential for inter-municipal competition



Selective Sales Taxes



- Motor vehicle tax: benefit-related; reduces road use
- Fuel tax: benefit-related; reduces road use
- Hotel tax: pays for services to tourists and visitors
- Alcohol tax: discourages use of alcohol; could be used to cover a portion of policing costs



Selective Sales Taxes

- Benefit principle
- Can affect consumer behavior e.g. vehicle taxes reduce automobile use
- Economic distortions – small base so rates may be high; high rates increase potential for evasion



International Experience



- More than 80% of tax revenues from personal and corporate income taxes in Belgium, Germany, Switzerland
- More than 80% of tax revenues from property taxes in Australia, Canada, US
- Sales taxes are levied mainly by cities in the US
- Mix of taxes in Austria and Spain (40% of local tax revenues from sales tax in Spain and almost 30% in Austria)

A Mix of Taxes



- Increases revenue elasticity
- Allows local governments to be more responsive to citizens
- One tax may create distortions offset by a mix of taxes

Intergovernmental Transfers



- Large cities have less need to rely on unconditional transfers than smaller cities because they have greater revenue raising capacity
- There is a case for transfers for large cities where:
 - they are providing services such as health and education
 - services spill over metropolitan boundaries (e.g. regional transportation)

How do you pay for infrastructure?



DIFFERENT INFRASTRUCTURE – DIFFERENT FISCAL TOOLS



Taxes

User fees

Borrowing



short asset life
(police cars,
computers)

identifiable beneficiaries
(transit, water)

large scale assets
with long life
(roads, bridges)

DIFFERENT INFRASTRUCTURE – DIFFERENT FISCAL TOOLS



Development charges



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

P3s



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

Land value capture
taxes



increase property values
(transit)

Borrowing



- Synchronizes costs and benefits over time
- Allows for immediate benefit from infrastructure investment
- Allows municipalities to avoid large year-to-year fluctuations in local taxes
- Larger cities have greater ability to borrow without upper level assistance; higher credit ratings than small cities

Development Charges



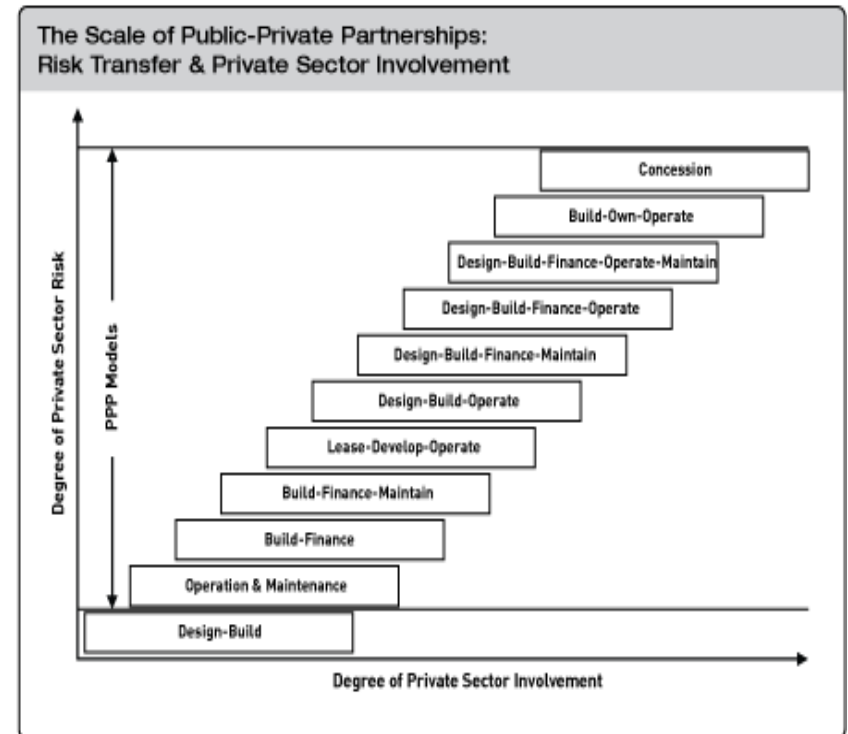
- One-time levy on developers to cover the growth-related capital cost associated with new development
- Off-site infrastructure (e.g. highways, sewer lines, etc.)
- Growth pays for itself
- Can differentiate charge by type of property (e.g. houses versus apartments) and by location



Public-Private Partnerships



- Private sector role can vary
- Private sector expertise and experience
- Competition can lower municipal costs
- But:
 - Potential loss of control for public sector
 - Private borrowing costs may be greater than public
 - Need realistic allocation of risk between public and private sector

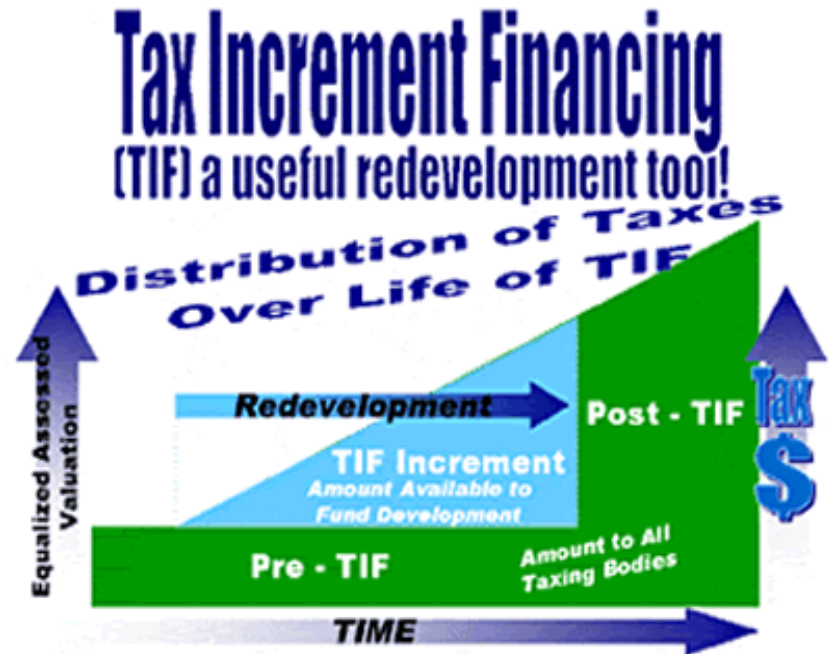


The Canadian Council for Public-Private Partnerships

Land Value Capture



- Increase in land value resulting from public investment is recouped by public sector for public purposes
- Used in Latin America; Tax increment financing (TIF) used widely in US jurisdictions
- What if forecast revenues not generated?



Are Large Cities Treated Differently?



- No comparable data on city finances
- City-states (e.g. Berlin, Hamburg, Bremen, Brussels) are assigned state and local responsibilities and revenues
- Some cities have special taxing powers (e.g. land transfer taxes in Toronto; additional taxing powers in New York City)



Taxes in Three Cities

Toronto	Berlin		New York City
Property tax	Land (state) taxes and tax shares:	Land (state) plus local shares:	General property
Land transfer tax	Share of corporate income tax	Personal income tax	General sales
Vehicle registration tax (cancelled)	Share of capital income tax	Business tax	Personal income
Billboard tax	Real estate transfer tax	Local taxes:	General corporation
	Motor vehicle tax	Real estate tax	Commercial occupancy
	Inheritance tax	Entertainment tax	Banking corporation
	Tax on betting and lotteries	Dog tax	Utility
	Fire protection tax	Second home tax	Unincorporated business
	Beer tax		Real property transfer
			Mortgage recording
			Tax audit revenues
			Cigarette
			Hotel

Concluding Comments



- Large metropolitan areas should be able to raise and spend budget themselves; reduce dependence on transfers
- May need transfers for health and education
- Those who benefit from expenditures should pay taxes/fees
- User fees for services where beneficiaries identified; local taxes for services with collective benefits

Concluding Comments (cont'd)



- Local tax rate setting
- Mix of taxes
- Range of tools to pay for infrastructure:
(borrowing, development charges, tax
increment financing, public-private
partnerships)