Financing Municipal Services for Sustainable Development – "Getting the Prices Right"

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Introduction

- Major cities around the world are experiencing rapid population growth
  - Pressure to provide services
  - Pressure to preserve farmland, open spaces, natural resources
- "Smart growth", "sustainability" – recognize the need to respond to growth pressures and pay for services on the one hand and protect the environment on the other

Theme of Presentation

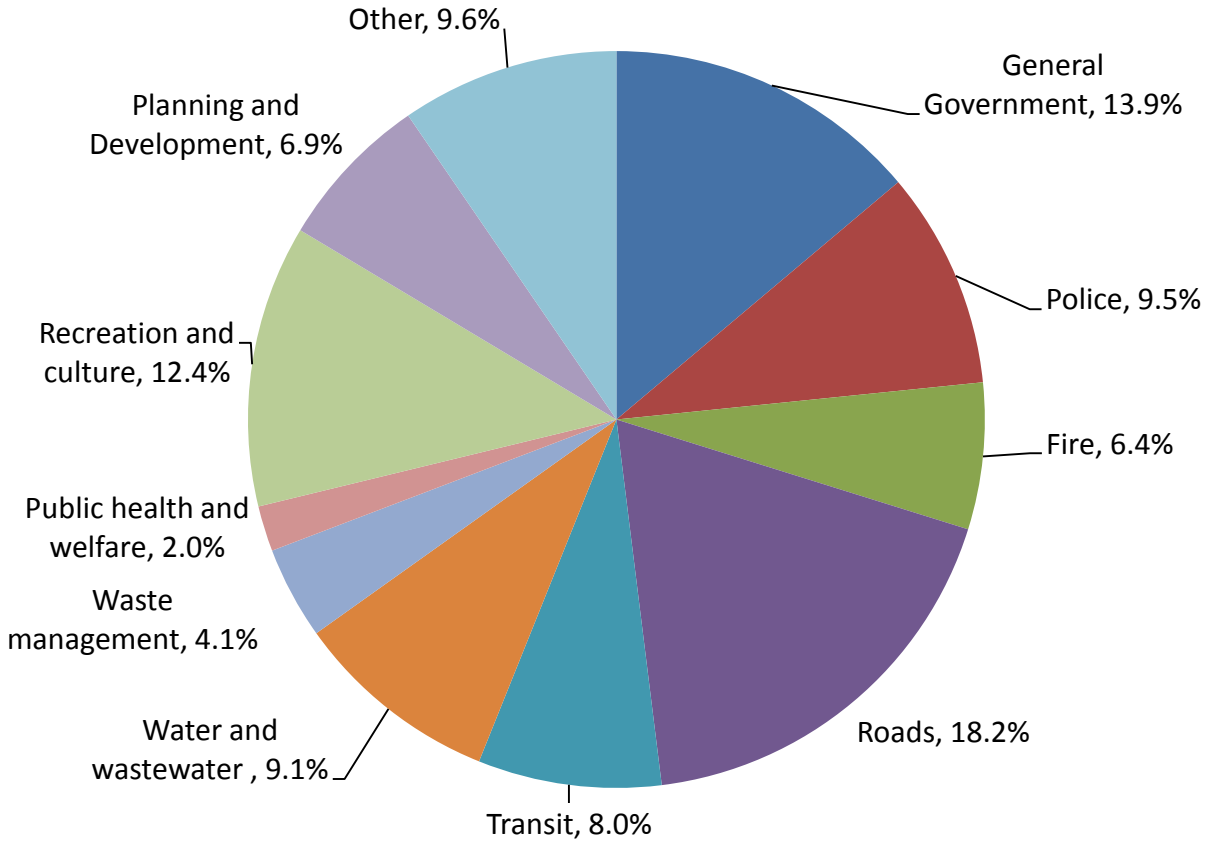
- If cities want to promote sustainable development, they need to think about how they pay for services
- Need to price services correctly and not subsidize inefficient development
- **"The city is a distorted price system"**

  (Wilbur Thompson, *Psychology Today*, 1968)

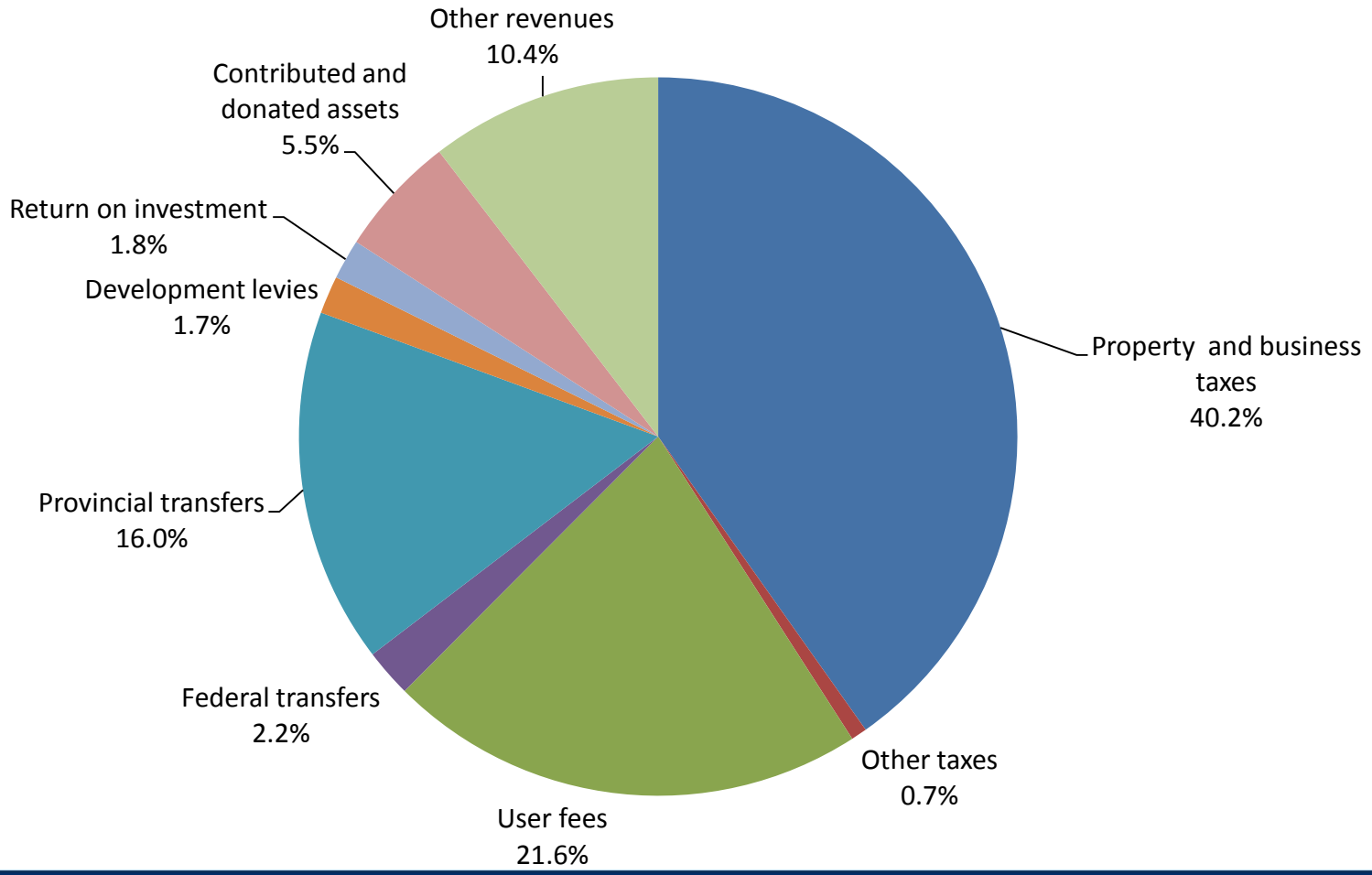
Outline of Presentation

- Municipal expenditures and revenues – Alberta municipalities
- Role of municipal finance in sustainable development
- Focus on specific revenue tools and impact on sustainable development:
  - User fees
    - Road pricing
    - Parking levies
  - Property taxes
  - Development levies

Distribution of Municipal Expenditures, Alberta 2012



Distribution of Municipal Revenues, Alberta, 2012



Role of Municipal Finance

- Municipal financial tools (e.g. property taxes, user fees, development levies) are generally not neutral with respect to development patterns
  - in some cases, they work together with planning tools to achieve sustainable development objectives
  - in other cases, they do the opposite

“Getting the Prices Right”

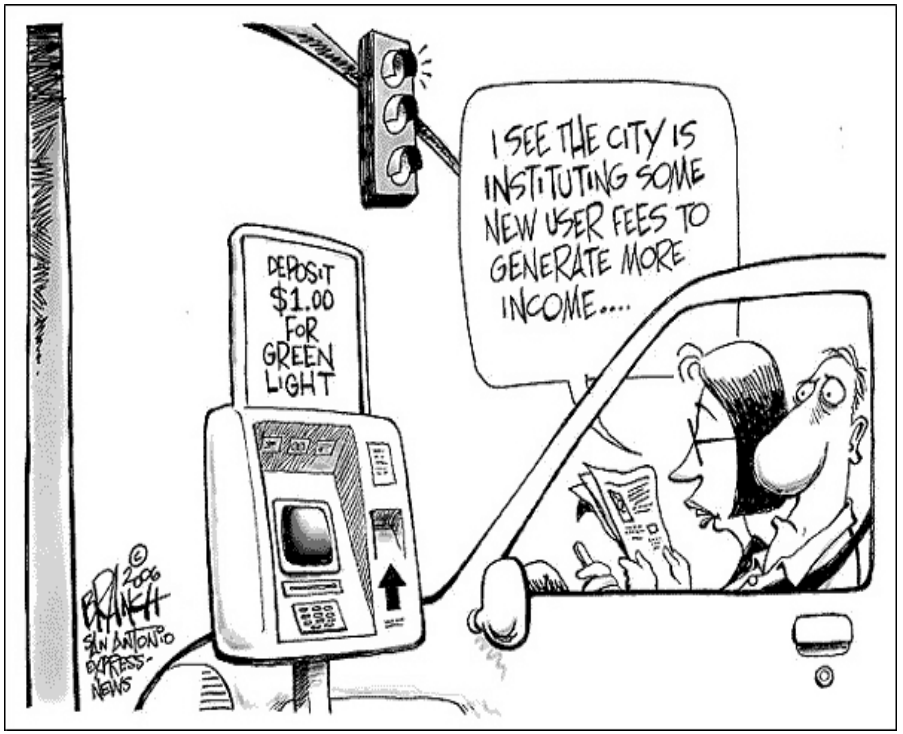
- Incorrect pricing of urban services has been at the root of a number of urban problems... including sprawl
- Marginal cost pricing -- higher fees are charged to those far away from existing services; if use average cost, subsidizing sprawl
- Pricing services correctly results in efficient use of services as well as more efficient land use

Pricing Services Correctly

- Examples:
  - User fees
    - Road pricing
    - Parking levies
  - Property taxes
  - Development levies

User Fees

- Signals what people are willing to pay for
- Need to be able to identify the beneficiaries and exclude those who don't pay
- Appropriate for water, sewage, garbage collection, highway improvement (tolls), public transit…



User Fees

- "Getting the prices right" means charging user fees that reflect the marginal cost -- the additional cost imposed by the user
- Allows governments and citizens to make efficient decisions about how much to provide and how much to consume

User Fees

- When users do not pay the marginal cost:
  - They overuse the system (so we think we need more roads or other infrastructure)
  - Encourages inefficient uses of land

User Fees

- BUT user fees are not used as much as they could be and are poorly designed
  - Not popular with citizens, politicians, administrators
  - Difficult to calculate marginal cost; difficult to exclude those who don't pay
  - New technology can help (e.g. roads and parking)

Road Pricing

- Highway users do not look at external costs (congestion and pollution); therefore over-use highways relative to what is economically efficient
- Under-pricing of auto congestion externality results in excessive dispersion – inefficiently low residential densities and sprawl

Road Pricing

- Road toll – incentive to make efficient decisions with respect to modal choice, trip frequency, trip timing, route choice (but not driving care!)
- Examples – London, Singapore, Toronto
- Need alternatives e.g. bus transit in London
- Technology makes it easier
- Maybe toll new roads or HOT lanes

Parking Levies

- Free parking provides wrong incentives – to use cars and park for the day in central city
- Cruising for spaces wastes time, fuel, creates traffic congestion, accidents, pollution
  - One study shows cars cruising for free parking contribute over 8% to total traffic
- Parking fees can vary with duration and location of parking, time of day

Property Taxes

- Major source of municipal revenue in Alberta and across Canada
- Levied on residential, commercial and industrial properties
- Tax levied on market value of property (land and buildings)

Property Taxes

- Some say the property tax reduces density – any investment that increases property value will increase the tax
- Others say it increases density because the tax is shifted onto consumers and leads to a reduction in the size of homes
- Property tax policy can reduce density:
  - E.g. Tax often favours single-family homes over apartments

Development Levies

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

Development Levies

- Developers will develop at the efficient time and place if they face the full social cost of their development
- If levy differentiated by location, density, type of development – then efficient development
- A uniform charge will subsidize inefficient land uses

Final Comments

- Need to create the right incentives for sustainable development
- Pricing services correctly (e.g. through user fees, property taxes, development levies) creates the right incentives for efficient use of resources and efficient land use