

Toronto's Competitive (Dis)advantage? Using Policy Levers Effectively

Notes for a Presentation to Roundtable on Economic Competitiveness and Social Cohesion Sponsored by the City of Toronto

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April 5, 2007

Introduction

- Previous speakers have discussed the need to link land use planning, economic development, cultural policy, and housing. They stopped short of the need to link all of these policies with municipal financial tools. My presentation is about linking municipal financial tools to other policies of the city.
- The discussion of economic competitiveness highlighted an important role for the city: to provide the services that attract, support, and retain firms and knowledge workers. These services not only include “hard” services such as roads, water, and sewers but they also include “soft” services that enhance the quality of life in the city. These services include, for example, parks, recreational facilities, arts and cultural facilities, and social services.
- I am going to talk about how the city pays for these services, not with the usual focus of whether they have enough tools and resources, but rather how their use of their existing tools affects economic competitiveness and social inclusion.
- Where people choose to live (in the city core, in the inner suburbs, or in greenfield suburbs), how they get to work (walking, by car, or by transit), how much water they consume, how much garbage they generate are all affected, at least to some extent, by municipal financial tools. Where businesses choose to locate is also influenced by fiscal tools.
- The theme of my presentation is that financial tools need to create the right incentives and they need to be consistent with other city policies. I will illustrate this theme with examples of existing financial tools (property taxes, user fees) plus two new tools (tax increment financing, public-private partnerships).

Property Taxes

- Property taxes account for 41 percent of the city's revenues. The property tax is levied on residential, commercial and industrial properties. It is levied as a tax rate multiplied

by the tax base; the tax base throughout Ontario is market value assessment (now to be assessed every four years).

- The property tax rate in Toronto is higher on non-residential properties compared to residential properties (the over-taxation of non-residential properties is common throughout the world as my review of property taxes in 25 countries suggests; see *International Handbook of Land and Property Taxation*, UK: Edward Elgar, 2004, co-edited with Richard Bird).
- Does this matter?
- Studies show that non-residential properties use fewer services than residential properties and therefore should pay fewer taxes than residential properties. Businesses are subsidizing residential properties (for example, a recent study by MMK in Vancouver shows that businesses there use 33 percent of municipal services and pay 52 percent of municipal property taxes). When the taxes are greater than the benefits from municipal services, there is an extra cost of doing business which can lead to lower economic activity – these costs can affect economic competitiveness.
- The non-residential tax rate in Toronto is also high relative to other municipalities in the GTA.
- Does this matter?
- Studies on business location suggest that property taxes do not matter between regions but they do matter within regions. In other words, if a business is looking at locating in Toronto or Buffalo, the most important factors will be access to skilled labour, access to universities, proximity to the airport, road links, etc. The property tax would not be as important as these other factors. If a business chooses to locate in Toronto, however, where it locates within the GTA may be affected by property taxes. Whether the business is on the north side of Steeles Avenue or the south side, for example, factors such as access to skilled labour or proximity to the airport will be comparable. Property tax differentials may, however, have an impact on their location decision.
- The good news is that the Toronto is reducing its non-residential tax rate (from 4 times the residential tax rate to 2.5 times the residential rate) over the next 15 years. In the recent provincial budget, it was announced that the provincial government will be reducing the business education tax rate for all municipalities in Ontario.

User Fees

- User fees are levied by the city for water, sewers, transit, recreation, and some social services. User fees account for 14 percent of the city's revenues. I am going to focus on user fees for two services: garbage and roads.

- User fees for garbage collection would discourage garbage. This policy goes to the liveability of the city and the environmental agenda. A form of user fee/tax is being proposed in Toronto but the details are not yet available. Charging for garbage collection and disposal is a good idea.
- Road pricing is a user fee that should also be seriously considered. Currently, automobile users are not charged the full cost of using the roads. Drivers pay for gas, insurance, license, and their own time but they do not pay for the congestion costs they impose on others or the pollution they generate. Road tolls on the 400 series highways would reduce automobile use and reduce congestion.
- Let me be clear that I am not recommending a congestion charge along the lines used in London, England. Unlike London, the congestion problem in Toronto is not in the downtown core; the congestion problem in Toronto is on the highways. These tolls should be levied by the Greater Toronto Transportation Authority (GTTA) because it is the regional roads and not the local roads that are congested.
- Tolls would reduce gridlock and that would increase economic competitiveness. Estimates indicate that \$2 billion is lost to the GTA economy every year from congestion.
- If these revenues were put towards transit, it could make it easier for those without cars to get to work. Road pricing could increase economic competitiveness and reduce social exclusion.
- Vehicle registration fees have been proposed for the city. These fees would discourage automobile use but are not as good as tolls because they do not vary by the time of day or by the location of the travel. The fee is the same if you are driving on a dirt road at 2:00 a.m. or on the 401 at rush hour.

Tax Increment Financing (TIF)

- TIFs are used in cities in 48 US states to revitalize downtown neighbourhoods. Funds are used for remediation costs, transit, and other infrastructure costs. TIFs are being considered in Toronto to revitalize downtown neighbourhoods and to finance the proposed new subway line.
- How do TIFs work?
- They generally follow a set of procedures. First, a TIF district is proposed where the geographic boundaries reflect the area that is in need of redevelopment. The annual property tax revenue accruing to all taxing authorities within the district (in Toronto, this would be the city for municipal property taxes and the province for education property taxes) is frozen at pre-revitalization levels. These are known as the base level property taxes. For a period of time, generally between 15 and 35 years, all or some portion of the incremental tax generated (above the base level) is set aside to be used for the redevelopment. Infrastructure investments and other improvements are made by the city

(or a redevelopment agency) by issuing bonds against the expected incremental tax increases. After the TIF period expires, tax revenues from the expanded assessment base again flow to the taxing authorities.

- In essence, the expected future increase in property taxes (resulting from the expected increase in property values) is used to back the bonds issued to finance the infrastructure today. Although there are some potential problems associated with using TIFs, they are a way to get the infrastructure built.

Public-Private Partnerships

- TIFs are generally used to revitalize downtown neighbourhoods. The inner suburbs are also in need of infrastructure investment in community and recreation facilities, for example. As other speakers have indicated, poverty is increasing in the inner suburbs but most of the services are located in the downtown. The city does not appear to have enough funds to invest in this infrastructure in all of the neighbourhoods that need it.
- A way to get that infrastructure is to involve the private sector in building the community facilities. The private sector could provide the needed capital for these facilities. The city could still have control over the services provided in those facilities to ensure access to families, for example.

Concluding Comments

- The financial tools that the city uses (or could use) not only bring in revenues to the city, they also affect people's behaviour. We need to make sure that we are creating the right incentives for people and businesses; we need to make sure that the city's financial tools are not working against other objectives of the city (such as economic competitiveness, social inclusion, and the environmental agenda).
- Some good things are happening in the city: the city is reducing property taxes on non-residential properties over the next 15 years; it is also considering applying user fees for garbage and using TIFs to revitalize downtown neighbourhoods.
- Other suggestions that should be considered include: road tolls to be levied by the GTTA on the 400 series highways to be used for transit and involving the private sector in building community facilities in the inner suburbs.