



# The Fiscal Health of Ontario Municipalities

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**MUNK  
SCHOOL  
OF  
GLOBAL  
AFFAIRS**



**UNIVERSITY OF  
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# Outline of Presentation

- The fiscal health of municipalities
  - What is it?
  - Who cares and why?
  - How is it measured?
- Assessing the fiscal health of Ontario municipalities
  - How has it been assessed?
  - What did we do?
  - What did we find?
- Toronto's fiscal health
- Paying for services and infrastructure



# THE FISCAL HEALTH OF MUNICIPALITIES





# What is “Fiscal Health”?

- The ability to meet financial and service obligations now and in the future
- Looks at the relationship between levels of expenditure requirements and revenues at a point in time as well as the relationship between growth rates in expenditures and revenues



# Who Cares and Why?

- Citizens – Will services be disrupted? Will taxes or user fees go up?
- Local governments – Can they meet expenditure requirements with existing revenues?
- Provincial governments – Will they be on the hook for bankruptcies? Who should receive transfers?
- Credit rating agencies – Can municipalities repay debt?



# Different Reasons, Different Measures

## Financial Management (PSAB)

- Sustainability (maintain services / meet obligations without increasing taxes or debt)
- Flexibility (ability to increase debt or taxes)
- Vulnerability (transfers or external risks)

## Credit Ratings

- Economic strength
- Financial strength
- Debt profile
- Governance & management structure

## Fiscal Distress

- Structural (long term debt)
- Economic (erosion of the tax base)
- Demographic (population decline)
- Institutional (management factors)

## Equalization Transfers

- Expenditure need (demographics, socioeconomic characteristics, geography, etc.)
- Fiscal capacity (size of tax base)



# ASSESSING THE FISCAL HEALTH OF ONTARIO MUNICIPALITIES





# Previous Measures in Ontario

- Provincial-Municipal Fiscal and Service Delivery Review (PMFSDR) 2008
  - ❑ Provincial-municipal exercise
  - ❑ 26 indicators covering six categories: property tax, assessment base, municipal costs, demographics, economic and financial
- Too many indicators; methodological issues with composite scores



# Previous Measures in Ontario

- Ontario Municipal Partnership Fund (OMPF)
  - ❑ Unconditional transfer introduced in 2005
  - ❑ Support rural and northern communities; municipalities with relatively high social program costs; rural communities with policing costs; and municipalities with weak assessment bases.
- Provincial redesign in 2013 based on a Municipal Fiscal Circumstances Index (MFCI)



# Measures in Ontario To Measure Fiscal Circumstances

## □ Primary indicators

- Weighted assessment per household
- Median household income

## □ Secondary indicators

- Average annual change in assessment (new construction)
- Employment rate
- Ratio of working age to dependent population
- Percent of population above low-income threshold



# IMFG Study (Slack, Tassonyi, Grad)

- 30 Ontario cities
- Data from 2000-2011
- Constructed lower tiers (where appropriate for comparison purposes)
- Measured in 2000 constant dollars



# Municipalities in this Study

- 30 municipalities in the sample (plus 6 Regions):
  - ❑ 13 Single Tiers
  - ❑ 17 Lower Tiers
- Largest municipalities: from 75,000 (Sault Ste. Marie) to 2.8 million (Toronto)
- North, south, east ,west
- Main data source: MMAH Financial Information Returns (2000-2011)



# Measures of Fiscal Health

- **Operating Revenues**

- Own-source revenues/total revenues
- Transfers/total revenues
- Taxes per capita

- **Expenditures**

- Total operating expenditures per capita
- Total capital expenditures per capita
- Capital expenditures/operating expenditures



# Measures of Fiscal Health

- **Debt Indicators**

- Total debt burden per capita
- Debt charges per capita
- Debt charges /operating expenditures
- Debt charges/own-source revenues (25% provincial borrowing limit)

- **Fiscal Indicators**

- Debt to tax ratio
- Taxes receivable as a per cent of current taxes levied

- **State of Capital Assets**

- Net book value as % of capital cost



# Interpretation of Measures

- Does a high debt burden signal a problem for a municipality or does it reflect important investments in needed infrastructure?
- Is a high dependence on provincial transfers good or bad? – adds to revenues (and ability to pay back loans) but less local fiscal autonomy increases vulnerability



# Summary of Findings

- Large Ontario municipalities have managed their finances conservatively; mostly rely on own-source revenues
- Debt service is being met
- Tax effort has been relatively stable but concerns for municipalities with declining tax bases
- Don't know if infrastructure and quality of services are deteriorating; municipalities could be fiscally healthy but face significant infrastructure challenges



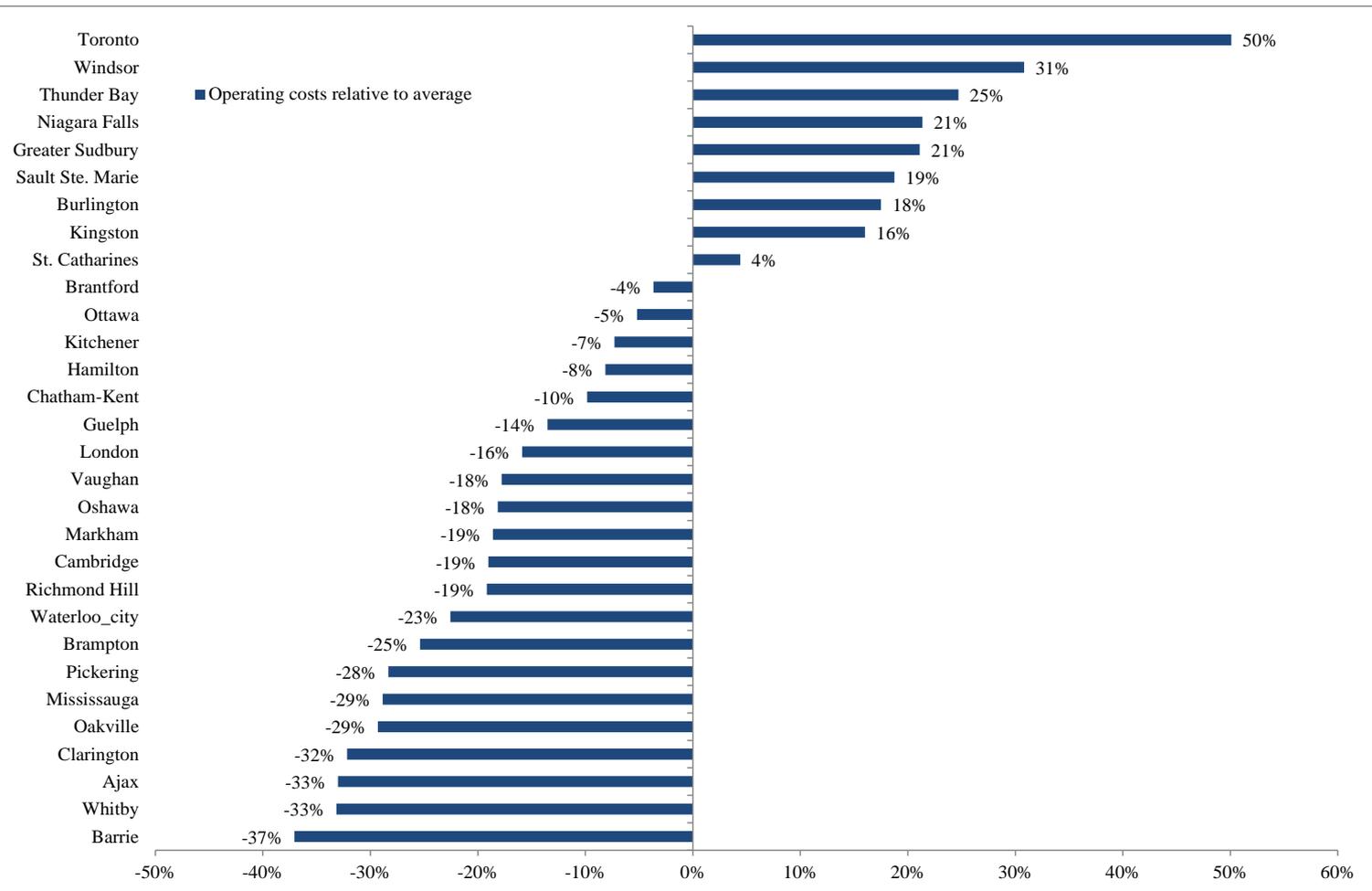
# Is There a Fiscal Gap?

- Fiscal gap – the gap between expenditure need and revenue-raising capacity (the “need-capacity gap”)
- Study by Slack, Tassonyi and Grad (2013)
- Followed other academic models from the US to approximate relative fiscal condition [Ladd and Yinger (1989), Chernick and Reschovsky (2006)]
- Calculated an ‘expenditure need’ and ‘revenue-raising capacity’ measure for each of the 30 cities
- Result is a *relative* measure based on the sample rather than an *absolute* measure for each city



# Expenditure Need and Fiscal Capacity

- Expenditure need is measured as the amount a municipality has to spend to provide a standard quality of public services given the costs it faces
- Regression equation on expenditure need:
  - Higher per capita incomes and dependency ratios place pressure on municipal expenditures per capita
- Fiscal capacity:
  - Higher per capita assessment provides capacity to finance relatively more spending



<b>Measure of Fiscal Health</b>						
	<b>Revenue</b>	<b>Expenditure</b>		<b>Relative</b>		
	<b>Raising Capacity</b>	<b>Need</b>	<b>Capacity - Need</b>	<b>Fiscal Health</b>	<b>Rank</b>	
Oakville*	2,461	1,562	899	1,473	1	
Vaughan*	2,356	1,816	540	1,114	2	
Mississauga*	2,078	1,571	507	1,081	3	
Pickering*	1,590	1,583	7	581	4	
Markham*	1,765	1,798	-34	540	5	
Richmond Hill*	1,725	1,786	-60	514	6	
Barrie	1,329	1,390	-61	513	7	
Toronto*	3,246	3,315	-69	505	8	
Whitby*	1,348	1,476	-129	445	9	
Cambridge	1,620	1,789	-169	405	10	
Guelph	1,723	1,910	-187	387	11	
Ajax*	1,205	1,480	-274	300	12	
Brampton*	1,371	1,648	-277	297	13	
Ottawa	1,723	2,094	-371	203	14	
Clarington*	1,109	1,499	-389	185	15	
Burlington*	2,184	2,596	-412	162	16	
London	1,292	1,858	-566	8	17	
Oshawa*	1,234	1,808	-574	0	18	
Hamilton	1,378	2,029	-651	-77	19	
Brantford	1,390	2,128	-738	-164	20	
Kitchener	1,209	2,048	-839	-265	21	
Chatham-Kent	1,029	1,991	-963	-389	22	
St. Catharines	1,230	2,306	-1,076	-502	23	
Kingston	1,439	2,562	-1,123	-549	24	
City of Waterloo	320	1,711	-1,391	-817	25	
Greater Sudbury	1,239	2,675	-1,437	-863	26	
Windsor	1,249	2,889	-1,641	-1,067	27	
Sault Ste. Marie	981	2,623	-1,642	-1,068	28	
Thunder Bay	1,001	2,755	-1,753	-1,179	29	
Niagara Falls	332	2,680	-2,348	-1,774	30	
<b>Average</b>	<b>1472</b>	<b>2046</b>	<b>-574</b>	<b>0</b>		
<b>Standard Deviation</b>	<b>586</b>	<b>501</b>	<b>85</b>	<b>659</b>		



# Conclusions on Fiscal Health

- Ontario municipalities have managed their finances conservatively
- Concerns for municipalities with declining tax bases outside the GTA
- Cannot tell whether infrastructure is deteriorating and quality of service is affected
- Municipalities could be fiscally health but face significant infrastructure challenges



# TORONTO'S FISCAL HEALTH



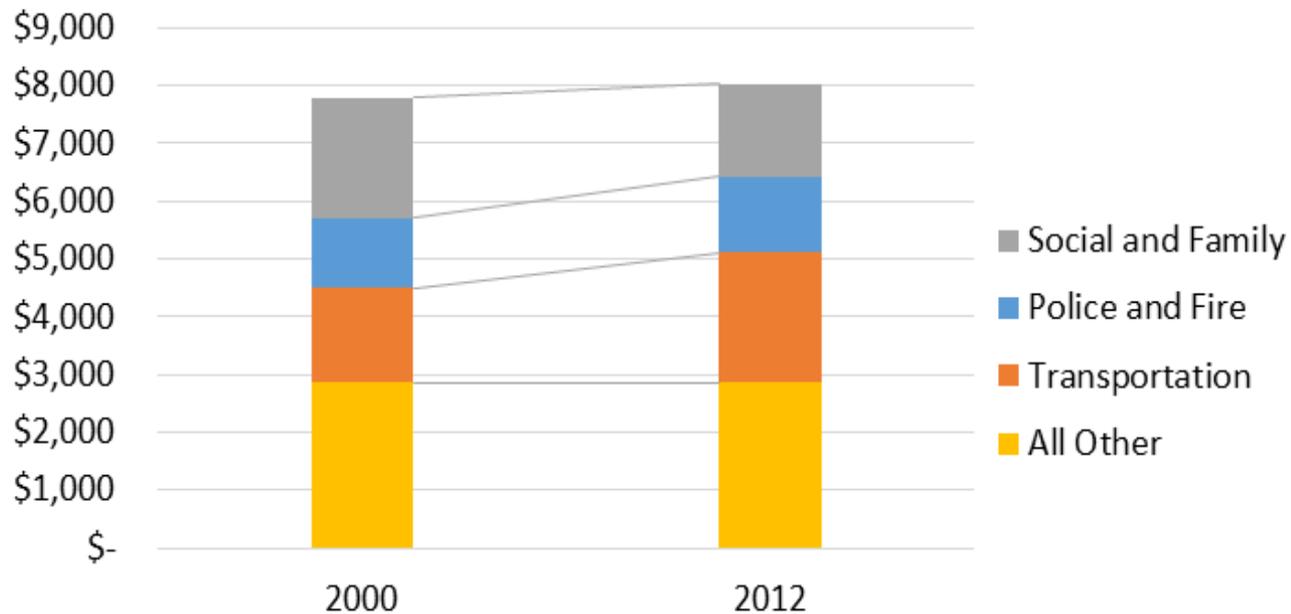


# Toronto's Finances

- Toronto does not have a spending problem
- Residential property taxes are low and have been growing less than the rate of inflation
- Toronto's debt is relatively manageable for a growing city
- City needs new revenues sources to maintain and invest in infrastructure

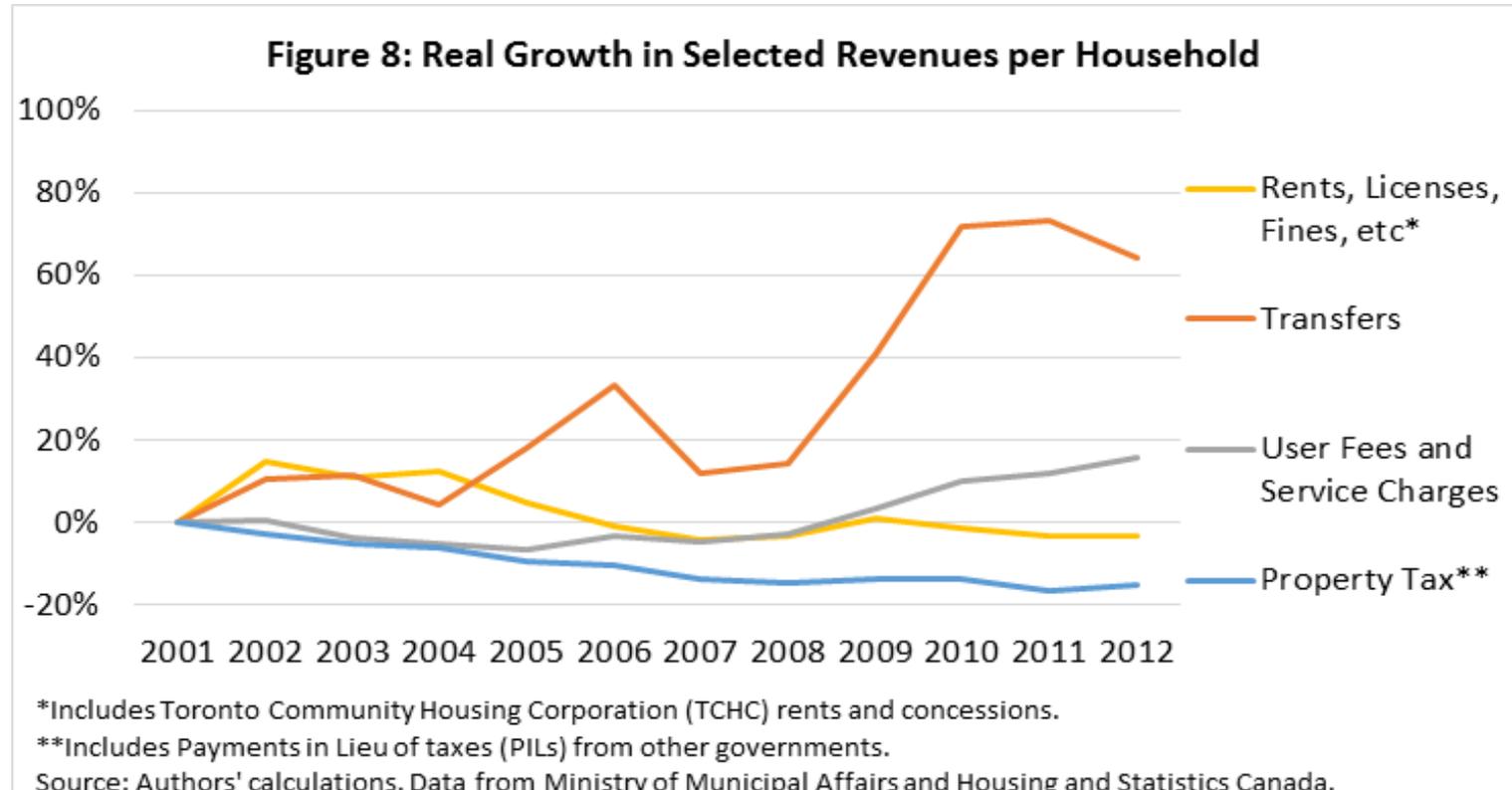
# Toronto's Finances

Figure 2: Toronto's Real Spending Per Household



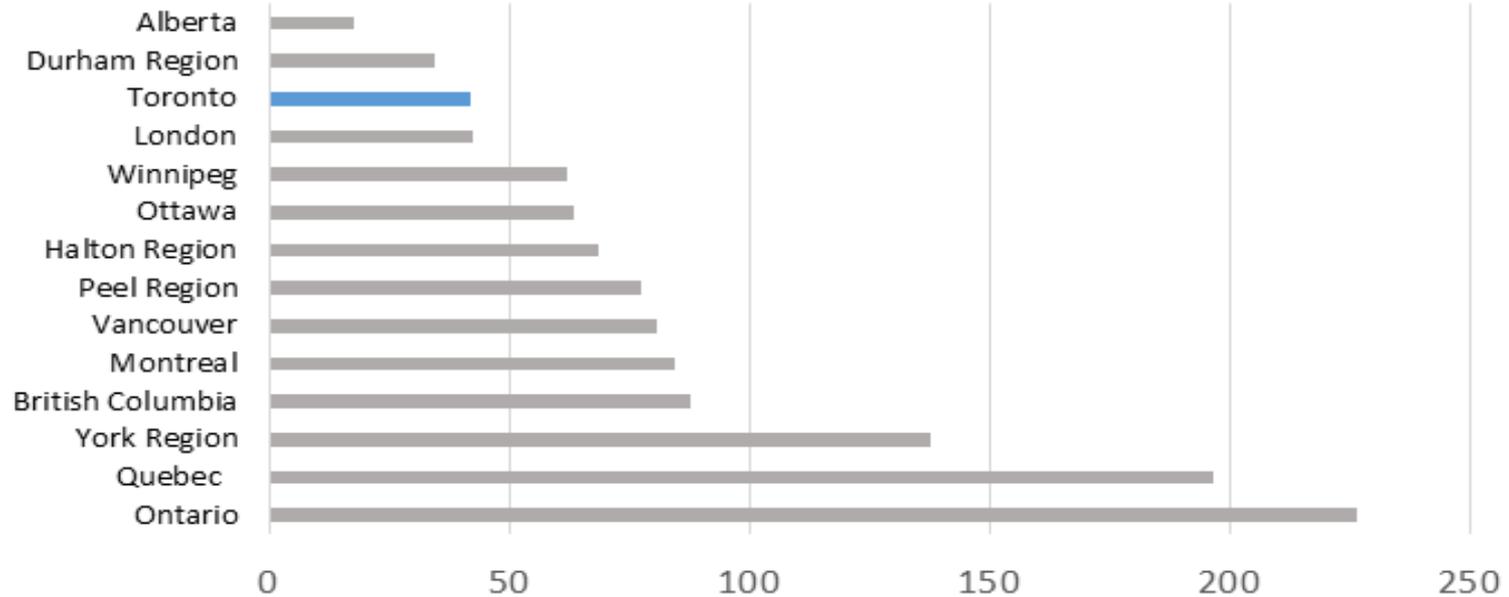
Source: Compiled by authors. Data from Ministry of Municipal Affairs and Housing Financial Information Returns and Statistics Canada.

# Toronto's Finances



# Toronto's Finances

Figure 19: Debt as % of Operating Revenue, 2012\*



\*Net Direct and Indirect Debt/Operating Revenue

Source: Moody's



# PAYING FOR SERVICES AND INFRASTRUCTURE





# Pricing Services Correctly

- How we pay for services affects our behaviour (e.g. how much water we consume, how much waste we generate)
- Pricing also affects nature, location and density of development
- Municipalities need to price services and infrastructure correctly – reduce demand for services and infrastructure



# Getting the Prices Right

- “The city is a distorted price system”  
(Wilbur Thompson, *Psychology Today*, 1968)
- 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 further away from existing services; if use average cost, subsidize sprawl
- New technology makes it easier to implement than in the past
- Pricing services correctly results in efficient use of services as well as more efficient land use



# DIFFERENT SERVICES – DIFFERENT REVENUE TOOLS

## Private

Water  
Sewers  
Garbage  
Transit

## Public

Police  
Fire  
Local parks  
Street lights

## Redistributive

Social assistance  
Social housing

## Spillovers

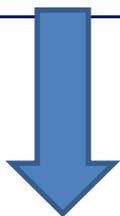
Roads/transit  
Culture  
Social assistance





# DIFFERENT INFRASTRUCTURE – DIFFERENT FISCAL TOOLS

## Taxes



short asset life  
(police cars,  
computers)

## User fees



identifiable beneficiaries  
(transit, water)

## Borrowing



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)

# Taxes in Other Major Cities

London	Paris	Berlin	New York
Council tax	Property tax on developed land	State taxes:	Real Estate Taxes
	Property tax on undeveloped land	Wealth tax	Payments in Lieu of Taxes (for property tax)
<b>Frankfurt</b>	Residence tax	Inheritance tax	
Property tax	Local economic contribution (on business premises and business value added)	Real estate transfer tax	Sales and Use Taxes:
Estate tax	Tax on refuse/garbage collection	Motor vehicle tax	General Sales
Business tax on income	Front walk sweeping tax	Racing and betting tax	Cigarette
Municipal share of sales tax	Parking fees	Beer tax	Commercial Motor Vehicle
Community share of sales tax	Electricity consumption tax	Fire protection tax	Mortgage
Other taxes, including gaming taxes and dog taxes	Real estate taxes (e.g. land transfer tax)		Stock Transfer
Key allocations made by the federal government		Local Taxes:	Auto Use
Land transfer tax allocation		Tax on land	
Trade tax allocation	<b>Tokyo</b>	Business tax	
	Metropolitan inhabitant tax on individuals, corporations, interest income	Trade tax allocation	Income Taxes:
<b>Madrid</b>	Enterprise tax on individuals and corporations	Entertainment tax	Personal Income
Property tax	Real property acquisition tax	Dog license fee	General Corporation
Business tax	Golf links tax	Second home tax	Financial Corporation
Vehicle tax	Automobile acquisition tax		Unincorporated Business Income
Tax on construction	Light-oil (gas-oil) delivery tax	State share of national taxes:	Personal Income (Non-Resident City Employees)
Tax on land value increase	Automobile tax	Wage tax	Utility
	Mine-lot tax	Assessed income tax	
Shared taxes:	Fixed assets tax	Non-assessed tax on earnings	Other Taxes:
Personal income tax	Special tax on land holding	Interest income tax	Hotel Room Occupancy
Value added tax	Hunter tax	Corporation	Commercial Rent
Excise taxes	Establishment tax	VAT	Horse Race Admissions
	Urban planning tax	Import VAT	Conveyance of Real Property
	Accommodation tax	Other	Beer and Liquor Excise
			Taxi Medallion Transfer
	Shared taxes:	Local share of state taxes:	Surcharge on Liquor Licences
	Local consumption tax	VAT	Refunds of Other Taxes
	Metropolitan tobacco tax	Wage and income tax	Off-Track Betting Surtax
	Local transfer taxes	Withholding	



# Concluding Comments

- By most measures, fiscal health of large Ontario cities appears good – with some exceptions
- But, how is the overall health of Ontario cities?
  - State of the infrastructure
  - Future pension liabilities, etc.
- Need to price services correctly
- Additional revenue sources?