Financing the Metropolis

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Introduction

- Metropolitan areas are generally characterized by many small, fragmented local governments and public agencies that provide local services in different parts of the region.

- Governance of these metropolitan areas is thus critical to coordinate service delivery across local government boundaries and to help shape a metropolitan identity.

- This presentation asks “how do you deliver services and pay for them on a metropolitan-wide basis when there are many local governments?”
Outline of Presentation

- Governance in metropolitan areas
  - Need to balance metropolitan and local interests
  - How do different governance models achieve this balance? How do they impact service delivery and taxes?

- Financing services in metropolitan areas
  - How should metropolitan services be paid for?
  - Which revenue tools?
Balancing metropolitan and local interests

- **Efficiency**
  - Ability to achieve economies of scale
  - Ability to reduce negative spillovers (externalities) across local boundaries

- **Equity**
  - Ability to share costs and benefits of services fairly across the metropolitan area

- **Accessibility and accountability for decision-making**

- **Local responsiveness/competition**
How well do different governance models achieve this balance?

- One-tier government model (fragmented local governments)
- One-tier government model (consolidated local governments)
- Two-tier government model
- Voluntary cooperation/special purpose districts
Fragmented One-Tier

- Many local governments operate in metropolitan area with independence in choosing public services and fees, taxes, and debt financing

- Local autonomy, responsiveness, competition

- Inability to address spillovers; lack of coordination of services, planning and economic development; cost of services not shared equitably across metropolitan area
One-Tier Consolidated

- Metropolitan government with powers to regulate service delivery and financing across metropolitan area

- Economies of scale; redistribution between rich and poor areas; coordination of service delivery; potential for more local influence with national policy makers; more unified actions for urban problems that do not respect political boundaries e.g. floods, crime, environmental pollution; more choices for efficient taxation

- Threat to local autonomy, responsiveness, and citizen engagement
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.)

- Empirical evidence shows economies of scale are service-specific:
  - Some economies of scale in central administrative functions; services with large capital inputs e.g. transportation, water and sewage systems

- Cities can also become too large – diseconomies of scale

- Canadian evidence: economies of scale for police at 50,000 people; for fire at 20,000 people (Found 2012)

- Evidence from Finland: economies of scale between 20,000 and 40,000 people (Moisio et al.)
Cost of Service Delivery

- Does consolidation/amalgamation reduce the cost of service delivery?
- May be able to achieve economies of scale and reduce duplication

BUT:

- harmonization of wages and salaries
- harmonization of service levels

- Case study of Toronto amalgamation 1998
Figure 1: Fire Expenditures Per Household - 1988-2008
Figure 2: Garbage Collection Expenditures Per Household - 1988-2008

- Metropolitan Toronto
- Scarborough
- Toronto
- East York
- North York
- York
- Etobicoke
- Metro Total
- Amalgamated Toronto

Linear (Metro Total)
Linear (Amalgamated Toronto)
Figure 3: Parks & Recreation Expenditures Per Household - 1988-2008
Figure 4: Libraries Expenditures Per Household - 1988-2008
Two-Tier Model

- Upper tier provides services that are region-wide, lower tiers provide local services

- Upper tier: economies of scale, redistribution, and internalize externalities

- Lower tiers: access and accountability

- Costs may be higher because of waste and duplication; may be less transparent and more confusing for citizens
Special Purpose Districts

- Single function placed under control of special district government; may have access to dedicated revenue stream (e.g. user fee or earmarked tax)

- Easy to create politically; easy to disband; local autonomy; economies of scale; address externalities

- Potential problems of accountability; redistribution not automatic
### Examples from Nine Federal Countries

<table>
<thead>
<tr>
<th>Country</th>
<th>Metropolitan Area</th>
<th>Governance Model</th>
</tr>
</thead>
<tbody>
<tr>
<td>Australia</td>
<td>South East Queensland (Brisbane)</td>
<td>One-tier; strong state role</td>
</tr>
<tr>
<td></td>
<td>Perth</td>
<td>Fragmented local governments; strong state role</td>
</tr>
<tr>
<td>Brazil</td>
<td>Belo Horizonte</td>
<td>Voluntary cooperation; state government in charge of shared functions; inter-municipal cooperation</td>
</tr>
<tr>
<td></td>
<td>São Paulo</td>
<td>Special purpose districts; state role</td>
</tr>
<tr>
<td>Canada</td>
<td>Toronto</td>
<td>One-tier consolidated</td>
</tr>
<tr>
<td></td>
<td>Vancouver</td>
<td>Two-tier</td>
</tr>
<tr>
<td>Germany</td>
<td>Central Germany</td>
<td>Voluntary cooperation</td>
</tr>
<tr>
<td></td>
<td>Hamburg</td>
<td>Voluntary cooperation</td>
</tr>
<tr>
<td>India</td>
<td>Hyderabad</td>
<td>Amalgamation; special purpose agencies</td>
</tr>
<tr>
<td></td>
<td>Mumbai</td>
<td>Special purpose agencies</td>
</tr>
<tr>
<td>South Africa</td>
<td>Gauteng city region</td>
<td>3 metros; limited inter-municipal cooperation</td>
</tr>
<tr>
<td></td>
<td>Cape Town</td>
<td>One-tier consolidated</td>
</tr>
<tr>
<td>Spain</td>
<td>Barcelona</td>
<td>Two-tier</td>
</tr>
<tr>
<td></td>
<td>Madrid</td>
<td>Two-tier</td>
</tr>
<tr>
<td>Switzerland</td>
<td>Geneva</td>
<td>Purpose-oriented intergovernmental cooperation</td>
</tr>
<tr>
<td></td>
<td>Zurich</td>
<td>Purpose-oriented intergovernmental cooperation</td>
</tr>
<tr>
<td>United States</td>
<td>Louisville</td>
<td>Consolidated one-tier</td>
</tr>
<tr>
<td></td>
<td>Los Angeles</td>
<td>Fragmented one-tier</td>
</tr>
</tbody>
</table>
Findings from Governance Research

- Different models have worked in different places at different times
- Political boundaries rarely coincide with boundaries of the economic region
- Strong traditions of local autonomy make metro-wide cooperation difficult
- Special districts may work where metropolitan area is too large for a political structure
- Consolidation does not necessarily reduce costs but may make it easier to levy taxes over the metropolitan area
How to Pay for Metropolitan Services

- Connection between those who decide, those who benefit, and those who pay:
  - Expenditure responsibilities matched by revenue resources
  - Revenue capacities matched with political accountability
  - Benefit areas matched with financing areas
How to Pay for Metropolitan Services

- Taxes levied by local governments should fall on local residents or non-residents (commuters and visitors) who benefit from services

- The more closely spending and taxing decisions are linked by being made by the same body at the same time, the better government will be efficiency of service delivery

- Lack of metropolitan governing structure is a constraint in providing local services efficiently in metropolitan areas
Financing Large Metropolitan Areas

- User charges

- Taxes:
  - Property taxes
  - Income taxes
  - Payroll taxes
  - Vehicle and fuel taxes
  - Sales taxes
  - Business taxes

- Intergovernmental transfers

- Financing infrastructure:
  - Development charges
  - Public-private partnerships
  - Borrowing
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
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)
## Distribution of Own-Source Revenues, Shared Taxes, and Transfers (%)

<table>
<thead>
<tr>
<th>City</th>
<th>Own-source revenues (taxes, user fees, other own-source revenues)</th>
<th>Shared taxes</th>
<th>Intergovernmental Transfers</th>
</tr>
</thead>
<tbody>
<tr>
<td>London (2011/12)</td>
<td>26.2</td>
<td>35.0</td>
<td>73.9</td>
</tr>
<tr>
<td>Berlin (2010)</td>
<td>39.5</td>
<td>4.5</td>
<td>25.5</td>
</tr>
<tr>
<td>Madrid (2009)</td>
<td>58.5</td>
<td>9.5</td>
<td>37.0</td>
</tr>
<tr>
<td>New York (2011)</td>
<td>69.1</td>
<td>24.1</td>
<td>30.9</td>
</tr>
<tr>
<td>Paris (2011)</td>
<td>82.5</td>
<td>17.5</td>
<td>14.6</td>
</tr>
<tr>
<td>Tokyo (2010)*</td>
<td>82.3</td>
<td></td>
<td>7.7</td>
</tr>
</tbody>
</table>

Note: *Included in own-source revenues are some taxes over which the metropolitan government has limited flexibility over tax rate setting.
How Should Metropolitan Services be Financed?

- Metropolitan areas should have greater fiscal autonomy than other urban areas –
  - greater responsibility for local services
  - greater ability to levy own taxes, collect own revenues, and borrow for capital expenditures
  - less dependence on intergovernmental transfers

BUT

- they need a governance structure that will allow them to levy taxes on a metropolitan-wide basis
Final Comments

- Area-wide general purpose government to address public financing problems in metropolitan areas may not be attainable
- A two-tier metropolitan structure could foster a metropolitan identity, address metro-wide issues, while still retaining local autonomy
- Elected metropolitan governments could be viewed as service delivery areas and financing districts (matching taxes and expenditures, beneficiaries and payers)
- Room for metro-wide governments to contribute more own-source revenues to finance services in metro areas: user fees and taxes (e.g. property, income); less dependence on transfers