



➤ Governance and Finance of Large Metropolitan Areas: Which Institutional Setting is Needed to Secure Metropolitan Economic Growth?

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Enid Slack  
Institute on Municipal Finance and Governance  
Munk School of Global Affairs  
University of Toronto

**IMFG**  
Institute on Municipal  
Finance & Governance

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UNIVERSITY OF  
TORONTO

*“ As it was our origin, the city now appears to be our destiny. It is where creativity is unleashed, community solidified, and citizenship realized. If we are to be rescued, the city rather than the nation-state must be the agent of change.”*

Benjamin Barber, *If Mayors Ruled the World* (2013)

# Cities are engines of economic growth

- ❑ Cities are important drivers of productivity, innovation, and economic growth
- ❑ Need for “hard” services (water, sewers, and roads) and “soft” services (cultural facilities, parks, and libraries) to attract skilled workers
- ❑ Cities that fail to provide these services will lose their economic advantage

# Outline of presentation

- ❑ Why does governance matter?
  
- ❑ Governance models in metropolitan areas
  - ❑ Criteria for evaluating governance models
  - ❑ Five models of governance ... with examples
  - ❑ Evidence from OECD countries
  
- ❑ How to pay for metropolitan services
  
- ❑ Final observations on governance and finance

# Why does governance matter?

- ❑ Metropolitan governance is critical to how:
  - ❑ services are delivered efficiently
  - ❑ service delivery is coordinated across the metropolitan area
  - ❑ costs are shared
  - ❑ citizens access local government
  - ❑ local governments are responsive and accountable

# Why does governance matter?

- ❑ Metropolitan governance matters for service delivery:
  - ❑ **Transportation:** Need to coordinate transportation across municipal boundaries; need to ensure access to employment and services; need to coordinate transportation and regional land use
  - ❑ **Water:** Need to determine where treatment facilities will be located
  - ❑ **Solid waste:** Need to determine where garbage disposal sites will be located
  - ❑ **Policing:** Need to fight crime across municipal boundaries
  - ❑ **Social services, health and education:** Need to decide on level of expenditures and how to share costs

# Why does governance matter?

- ❑ Quality of the business environment affects investment and economic growth
- ❑ Impact on productivity – e.g. larger cities enjoy agglomeration economies
- ❑ Impact on productivity – e.g. fragmented governance could increase cost of doing business because of need to deal with many local offices, ineffective planning and congestion
- ❑ Coordination of economic development activities – reduce harmful competition within the metropolitan area

# Balancing regional and local interests: criteria to evaluate governance models

- ❑ 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

# Five models

- ❑ One-tier fragmented government structures
- ❑ One-tier consolidated government structures
- ❑ Two-tier government model
- ❑ City-state
- ❑ Voluntary cooperation/special purpose districts

*A metropolitan area can reflect more than one model*

# 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

# Fragmented One-Tier Structures

- ❑ Los Angeles – 200 cities and 5 county governments
- ❑ Geneva – 74 municipalities
- ❑ Sydney – 43 local councils
- ❑ Mumbai – 7 municipal corporations, 13 municipal councils, parts of two districts, more than 900 villages, 21 parastatals

*Examples of inter-municipal cooperation to follow*



# One-Tier Consolidated

- ❑ Metropolitan government with powers to deliver services and raise revenues across metropolitan area
- ❑ Economies of scale; redistribution between rich and poor areas; coordination of service delivery; internalizes externalities; more choices for efficient taxation
- ❑ Threat to local autonomy, responsiveness, and citizen engagement
  - ❑ Innovative mechanisms – open government; participatory budgeting
- ❑ Reduces competition among municipalities – weakened incentives to be efficient
- ❑ What is the appropriate boundary?

# Consolidated One-Tier Structures

- ❑ Cape Town – geographic boundary coincides with economic region
- ❑ Toronto – a city too big and too small
- ❑ Auckland – amalgamation in 2010 resulted in municipality covering entire metropolitan area plus rural areas



# Two-Tier

- ❑ Upper tier provides services that are region-wide; lower tiers provide local services
- ❑ Upper tier: economies of scale, redistribution, internalize externalities
- ❑ Lower tiers: access and accountability
- ❑ Costs may be higher because of duplication
- ❑ May be less transparent and more confusing for citizens

# Two-Tier Structures

- ❑ London – Greater London Authority plus 32 boroughs
- ❑ Barcelona – Metropolitan council plus 36 lower tiers
- ❑ Tokyo – Metropolitan government plus 23 special wards, 26 cities, 5 towns, 8 villages
- ❑ Seoul – Metropolitan government plus 25 districts



# City-States

- ❑ City and state powers
- ❑ Internalize externalities, region-wide taxation, broad-based taxes, enhanced borrowing powers
- ❑ Expansion of boundaries into other states is difficult
- ❑ Tensions between city-state governments and central government

# City-States

- ❑ Berlin, Bremen, Hamburg
  - ❑ more legal powers than cities but territory does not cover entire urban agglomeration
  
- ❑ Singapore
  - ❑ city-nation
  
- ❑ Shanghai



# Special Purpose Districts

- ❑ Single function placed under control of special district; 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
- ❑ No regional vision

# Special Purpose Districts

- ❑ Greater ABC Region in São Paulo (“bottom up”)
- ❑ Public company for transportation planning for metro area in Bogotá
- ❑ Parastatals in Mumbai delivering a range of services
- ❑ Regionally integrated public transport systems in Germany



# Evidence from OECD countries

- ❑ Review of governance structures in 275 metropolitan areas in OECD countries
  
- ❑ Main functions for metropolitan organizations:
  - ❑ regional economic development
  - ❑ spatial planning
  - ❑ transportation

Source: Ahrend, Gamper, and Schumann (2014)

# Evidence from OECD countries

- ❑ Few powers; small budgets
  
- ❑ Yet, where there are metropolitan organizations – metropolitan areas perform better than fragmented local governments:
  - ❑ denser
  - ❑ higher per capita GDP
  - ❑ attract more people
  - ❑ higher level of public satisfaction with public transport
  - ❑ lower levels of air pollution

Source: Ahrend, Gamper, and Schumann (2014)

# Evidence on governance and productivity

- ❑ Study of Germany, Mexico, Spain, United Kingdom, United States
- ❑ Fragmented governance structures tend to have lower levels of productivity (measured by wage premiums)
- ❑ A metropolitan area with twice the number of municipalities is associated with around 6 percent lower productivity
- ❑ Impact cut in half if there is a governance body at the metropolitan level

Source: Ahrend, Farchy, Kaplanis and Lembcke (2014)

# 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 at efficient 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



# 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)

# Tax incentives to pursue economic development goals

- ❑ Used to increase income and employment, expand tax base, revitalize distressed areas

BUT

- ❑ Impact depends on type of business activity (e.g. manufacturing versus retail)
- ❑ Impact depends on services provided
- ❑ Only a factor in intra-metropolitan and not inter-metropolitan location decisions
- ❑ Incentives lose effectiveness if other cities introduce them too

# 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 observations

- ❑ Different governance models have worked in different places at different times
  
- ❑ National and local context matter:
  - ❑ constitution
  - ❑ division of responsibilities and revenues
  - ❑ history of local autonomy
  
- ❑ Political boundaries rarely coincide with boundaries of the economic region
  
- ❑ Strong traditions of local autonomy make metro-wide cooperation difficult

# Final observations

- ❑ 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
- ❑ Need for strong regional structure that encompasses economic region; need to balance regional and local interests
- ❑ Governance and finance are linked – design effective metropolitan governance and then appropriate fiscal structure