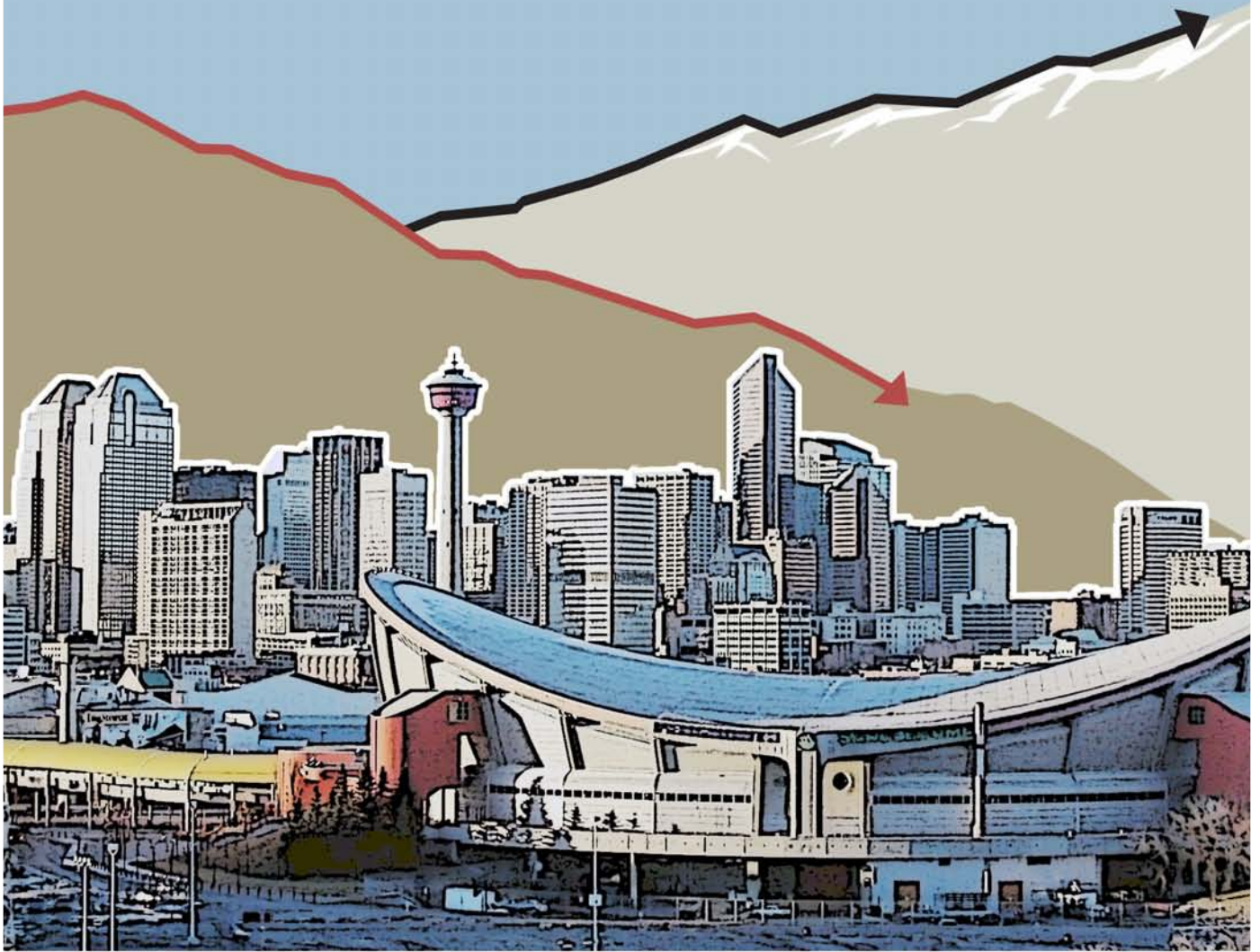
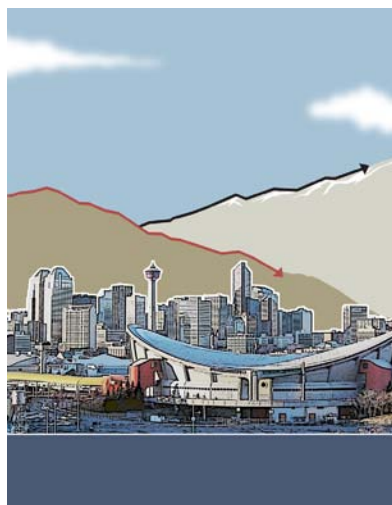


# No Free Lunch: Financing the Priorities of Calgarians



Parkland Institute • June 2010





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ISBN 978-1-894949-28-6

## Acknowledgements

The author thanks: Greg Flanagan, Diana Gibson, Jake Kuiken, Byron Miller and one anonymous reviewer for thoughtful reviews; Karen Sherlock and Scott Lingley for thorough and accurate copy editing and proofreading respectively; and Flavio Rojas for professional cover work and layout. The author takes sole responsibility for content.

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## About the Parkland Institute

Parkland Institute is an Alberta research network that examines public policy issues. We are based in the Faculty of Arts at the University of Alberta and our research network includes members from most of Alberta's academic institutions as well as other organizations involved in public policy research. Parkland Institute was founded in 1996 and its mandate is to:

- conduct research on economic, social, cultural, and political issues facing Albertans and Canadians.
- publish research and provide informed comment on current policy issues to the media and the public.
- sponsor conferences and public forums on issues facing Albertans.
- bring together academic and non-academic communities.

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## Executive Summary

How will the City of Calgary address its budgetary issues in coming years?

Will the City rely on property tax increases? Will it hope for and ask for higher levels of funding from the provincial government? Will it launch into an agenda of cuts to programs and services? Will it be lured toward privatization? Or will it explore new revenue options?

Fortunately, it is clear what Calgarians want. In the last several years, Calgarians have been surveyed and have participated in comprehensive, long-term visioning and planning processes. The imagineCALGARY Plan, which received the input of over 18,000 Calgarians, sets goals and strategies to make Calgary a green, equitable, community-minded city.

Calgarians' vision requires excellent public services and facilities. Economic and population growth also require increased public spending. So how will the City finance Calgarians' desires and support growth?

Fortunately, Calgarians understand that excellent public services and facilities carry a price tag, and they are willing to pay. Public opinion surveys show that Calgarians are far more concerned with a wide range of social and environmental issues than they are about taxes. More Calgarians want taxes maintained or increased than want them cut. Indeed, in the imagineCALGARY process, Calgarians voiced their opinions that the municipal tax basket should be expanded, diversified, more progressive and employed to achieve environmental and social goals.

Currently, the property tax is Calgary's biggest revenue source, which is unfortunate as it is a regressive tax that does not grow automatically with economic growth—and Calgarians prefer other options. And while grants from senior levels of government are nice to get, they can't be relied upon, particularly for operational spending. Grants are subject to the whim of senior governments, and can be cut when it is deemed expedient. Furthermore, they reduce transparency and accountability for tax dollars raised.

Public-private partnerships (PPPs or P3s) and privatization are often presented as a panacea, a way in which corporations will help the public create facilities and deliver services. However, the "free lunch" these arrangements are often touted as providing simply doesn't exist. Corporations aren't about to hand over money or provide services

or new facilities for free. Indeed, they tend to introduce new costs—ranging from CEO bonuses, to higher borrowing costs, to shareholder dividends, to lobbying and advertising costs. The vaunted “transfer of risk,” in which P3 private developers are said to absorb public risk, doesn’t come for free; it raises the price of the project. In the end, citizens pay for public services and facilities; it is not clear why they should be required to pay such additional costs.

Another course worth exploring, as suggested by Calgarians, is the development of alternative local revenue streams. In addition to providing revenues for important public investments, these alternative revenue sources can encourage improved environmental and social sustainability. By including “externalities” (social and environmental costs) in market prices, taxes, charges and user fees can correct market failure. They can also reduce excessive consumption (e.g. of energy, water, road space, etc.) and by doing so, reduce the capital and operational costs faced by municipalities.

While user fees got a bad name in the 1990s, when many regressive versions were created, the good news is that they don’t have to be regressive. They can be designed to be progressive in terms of consumption, income or wealth. And they can be designed to protect Calgarians with modest incomes.

Implementing some of these revenue adjustments may require provincial legislative support in some instances. The City of Toronto Act provides an example of a city being entrusted with a suitable degree of autonomy; Calgary is being held back, and reform at the provincial level would be appropriate.

Investing in public services and facilities has another substantial benefit. It creates jobs directly, by employing people to provide those services and facilities. It also creates jobs indirectly, in supplier industries. Finally, it creates induced employment in the industries that absorb spending from the above-noted workers.

The number of jobs by investment created varies from industry to industry. Compared to the oil and gas industry, investing in municipal government services creates far more jobs per dollar invested, as well as more GDP growth per dollar. Likewise, when governments cut public spending, a lot of people are thrown out of work—both in the public sector and the private sector—and economic growth is diminished. Tax cuts can potentially create jobs, but not as many as public spending creates.

In conclusion, it is clear that the City has realistic revenue options to support the priorities Calgarians have outlined, and to manage growth. Fortunately for City Council, Calgarians support the idea of exploring a new range of revenue sources. And fortunately for Calgarians, these sources can be designed wisely, so as to meet the revenue needs and also have positive effects on the environment and other areas.

In a democracy, it is important to take citizen preferences seriously. The City has the capacity and the political room to address its financial needs honestly. Calgarians are ready for a mature conversation about public services, facilities and revenues. Is the City?

## Introduction

How will the City of Calgary address its budgetary issues in coming years?

Will it rely on property tax increases? Will it hope for and ask for higher levels of funding from the provincial government? Will it launch into an agenda of cuts to programs and services? Will it be lured toward privatization? Or will it explore new revenue options?

It's clear what Calgarians want. They have said they want improvements to the City in many areas, ranging from transportation and waste management, to sufficient income and equity for their fellow citizens, to a clean environment and a sense of community well-being.

In the last several years, Calgarians have participated in comprehensive, long-term visioning and planning processes aimed at making Calgary a better place. The imagineCALGARY Plan<sup>1</sup> was developed with the input of more than 18,000 community members—one of the largest community visioning and consultation processes of its kind in the world.<sup>2</sup> The imagineCALGARY process created a 100-year vision for Calgary as:

*“...a community in which*

- We are each connected to one another. Our diverse skills and heritage interweave to create a resilient communal fabric, while our collective spirit generates opportunity, prosperity and choice for us all.*
- We are each connected to our places. We treasure and protect our natural environment. Magnificent mountain vistas and boundless prairie skies inspire each of us to build spaces worthy of their surroundings.*
- We are each connected to our communities. Whether social, cultural or physical, these communities are mixed, safe and just. They welcome meaningful participation from everyone, and people move freely between them.*
- We are each connected beyond our boundaries. We understand our impacts upon and responsibilities to others. Our talent and caring, combined with a truly Canadian sense of citizenship, make positive change across Alberta, throughout Canada and around the world.”<sup>3</sup>*

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1 “imagineCALGARY Plan for Long Range Urban Sustainability” (City of Calgary, June 2006), [http://www.imaginecalgary.ca/imagineCALGARY\\_long\\_range\\_plan.pdf](http://www.imaginecalgary.ca/imagineCALGARY_long_range_plan.pdf).

2 City of Calgary, “imagineCALGARY Plan for Long Range Urban Sustainability,” p. 194, [http://www.imaginecalgary.ca/imagineCALGARY\\_plan.php](http://www.imaginecalgary.ca/imagineCALGARY_plan.php).

3 “imagineCALGARY Plan for Long Range Urban Sustainability” op.cit. at p.1.

The plan aims to make Calgary “a model city, one that looks after the needs of today’s citizens and those to come.” It sets out 100-year goals and 30-year targets for each goal, in addition to strategies for each target. The goals range widely, including renewable energy,

sufficient incomes, affordable housing, equity and diversity, a clean environment, a sense of community and much more.

Following imagineCALGARY came the Plan It Calgary process—the creation of municipal development and transportation plans aligned with the vision and goals of imagineCALGARY. This process involved public opinion surveys, citizen workbooks, focus groups and other avenues for input. The result was two plans adopted in September 2009<sup>4</sup> that contain a 60-year vision and policies to implement that vision over the next 30 years.

Calgarians have done the work; they have discussed and decided what they want their community to look like. From these processes and plans it is clear that, like other Canadians, Calgarians care about their communities and the public services and facilities they depend on. To reach the ambitious goals of these plans, investment in public services and facilities will be required.

Even apart from new public investments needed to create such improvements, higher spending will be necessary merely to support Calgary's growth. The City will need to find revenues, one way or another, in order to maintain the current level and quality of services.

This short report first looks briefly at the views of Calgarians on public spending priorities and taxes and other revenues, as revealed by consultations and public opinion surveys.

It then considers revenue options for achieving the desires of Calgarians and addressing growth. Property taxes and provincial grants are discussed, along with some of their challenges. The claims made on behalf of privatization and public-private partnerships (P3s) are questioned, and some of their hidden costs are noted.

The report then outlines some revenue alternatives that could be adopted. It looks at how revenue systems can be designed to achieve social and environmental goals.

It goes on to consider the wider employment and economic benefits of investing in quality public services and facilities, including the benefits that accrue to the private sector (and the impact on the private sector of public sector spending cuts).

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4 "The City of Calgary Municipal Development Plan" (City of Calgary, April 2010), [http://www.calgary.ca/docgallery/BU/planning/pdf/municipal\\_development\\_plan/municipal\\_development\\_plan.pdf](http://www.calgary.ca/docgallery/BU/planning/pdf/municipal_development_plan/municipal_development_plan.pdf); Calgary Transportation Plan (City of Calgary, April 2010), [http://www.calgary.ca/docgallery/BU/planning/pdf/municipal\\_development\\_plan/calgary\\_transportation\\_plan.pdf](http://www.calgary.ca/docgallery/BU/planning/pdf/municipal_development_plan/calgary_transportation_plan.pdf).

## Financing the Priorities

Like other municipalities, Calgary has inadequate revenues to deliver on its goals and its citizens' desires. Furthermore, Calgary's growth has put pressure on its facilities and services. Calgary's population rose from 900,000 to 1.3 million in the last 14 years, and it is projected to surpass 1.5 million in the next seven years.<sup>5</sup> Continued economic growth itself will require increasing municipal support; in order even to maintain facilities and services at current levels Calgary will need to keep increasing its spending in certain key areas.<sup>6</sup> This will require additional revenues.

### *Are Calgarians willing to pay higher taxes?*

Whatever the myths and stereotypes may say, the facts are clear: Calgarians are not preoccupied with cutting taxes. They understand that excellent public services and facilities need to be paid for, and they are willing to pay.

A 2009 Ipsos Reid survey of Calgarians found that 75 per cent felt taxes should be maintained or increased.<sup>7</sup> Only 13 per cent felt taxes should be cut. Taxes are not a major preoccupation for Calgarians; only four per cent named taxes and fees as the most important local concern, falling behind infrastructure (25 per cent) and transit (16 per cent), as well as crime, education and health care.<sup>8</sup> Only five per cent felt that taxation had caused any worsening of the quality of life in Calgary, putting it at 10th place on that list of local concerns.<sup>9</sup>

A 2007 Canada West Foundation survey had similar results. It found that 80 per cent of Calgarians felt the City had too little or enough money to fulfill its responsibilities; only 13 per cent felt it had too much.<sup>10</sup> Another report noted that property taxes are 11th in the priority list for Calgarians, well behind traffic and transit, homelessness, the environment and air quality, among others.<sup>11</sup>

These survey results are consistent with public opinion surveys of Albertans more generally; year after year they rate public services as high-priority concerns, and taxes are way down the list.<sup>12</sup>

The imagineCALGARY process also addressed taxes. Calgarians had ample opportunity to discuss taxes, and to insist en masse that they be cut drastically. They didn't do so. The imagineCALGARY Plan shows what Calgarians really want in their tax system.

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- 5 Calgary Economic Development, "Demographics," <http://www.calgaryeconomicdevelopment.com/liveWorkPlay/Live/demographics.cfm>.
  - 6 This assumes that economic and population growth in Calgary will continue in the foreseeable future. If or when they eventually come to an end, there will be a different set of challenges to address. Hopefully, Calgary will have made the right investments.
  - 7 Maintained, 27 per cent; increased, 48 per cent-to maintain or expand services. Ipsos Reid, "The City of Calgary 2009 Citizen Satisfaction Survey," p. 27, [http://www.calgary.ca/docgallery/bu/customerservice/2009\\_citizen\\_satisfaction\\_survey.pdf](http://www.calgary.ca/docgallery/bu/customerservice/2009_citizen_satisfaction_survey.pdf).
  - 8 Ipsos Reid, "The City of Calgary 2009 Citizen Satisfaction Survey," op.cit. p. 5.
  - 9 Ibid p. 9.
  - 10 Enough, 41.3 per cent; too little, 38.5 per cent; too much, 13 per cent. L. Berdahl, "Looking West 2007, Segment 2: Urban Policy Priorities and Assessing Governments" (Canada West Foundation, April 2007), p. 5, [http://www.cwf.ca/V2/files/LW07\\_Urban\\_Policy\\_Priorities1.pdf](http://www.cwf.ca/V2/files/LW07_Urban_Policy_Priorities1.pdf).
  - 11 L. Berdahl, "City Views: An Analysis of the Looking West 2007 Survey" (Canada West Foundation, September 2007), p. 17, <http://www.cwf.ca/V2/files/LW07.6large.pdf>.
  - 12 NRG Research Group, "Issues of Importance in Alberta 2003-2009" Figure 2, "CBC Health Care Poll by NRG Research Group, September 2009" (CBC, October 5, 2009), <http://www.cbc.ca/calgary/features/healthcare-poll/poll-part1.html>. See also L. Berdahl, "Looking West 2007, Segment 2: Urban Policy Priorities and Assessing Governments" op.cit. p.8.

It speaks of

- diversifying the range of tax streams to reduce reliance on property taxes;
- making the tax system more progressive, to benefit lower-income individuals;
- using taxes to achieve environmental goals, e.g. through carbon and fuel taxes and incentives to redevelop vacant land in established areas;
- using tax incentives to achieve social goals, e.g. a living wage standard; and
- adjusting taxes to diversify the economy and encourage local businesses that support sustainability practices.

Clearly, a stripped-down public sector with greatly reduced taxes is not the agenda of Calgarians. Perhaps this is one of the reasons why voter turnout is so notoriously low in Alberta, particularly in municipal elections—voters aren’t particularly interested in what’s on the table.

What anti-tax zealots seem to ignore is that most people—including Calgarians—disagree with them. Taxes pay for public services that citizens value. The zealots like to portray taxes as somehow going down a black hole and providing nothing in return. This is a twist on the free lunch idea; instead of a lunch with no bill on the table, the zealots claim there is a bill on the table with no lunch being served.

Evidently, Calgarians don’t buy that story.

*“You can’t have low taxes and world-class services, no matter what the neo-cons tell you.”<sup>13</sup>*

### ***Property taxes and provincial transfers***

Given that tax cuts aren’t what Calgarians want, how should the City finance its increased future spending needs? Should it just go back to the well—i.e. raise property taxes and go asking for provincial money?

Do Calgarians want that? And would it work?

The biggest revenue source for Canadian municipalities, including Calgary, is the property tax. This is unfortunate, as property taxes are far from an ideal tax. First, they are regressive; lower-income families spend more of their incomes on property taxes than do higher-income families. And Calgary’s property taxes are among the more regressive in Canada.<sup>14</sup> Furthermore, property tax revenues are not sensitive to

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13 S. McKeen, “Superior services, low taxes can’t coexist-somebody has to pay” (Edmonton Journal, January 20, 2010), p. B1, <http://www.edmontonjournal.com/news/Superior+services+taxes+exist+somebody/2461764/story.html>.

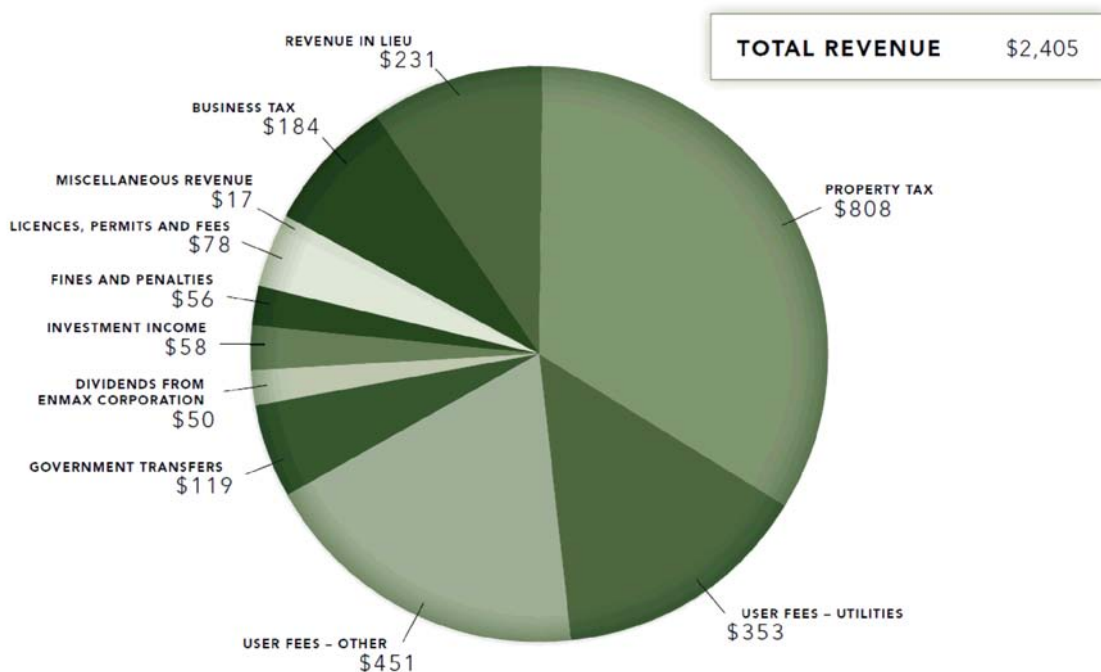
14 Idem.

growth; they do not automatically increase with economic growth, like income taxes do. For these reasons, many municipal councillors are reluctant to raise property taxes.

*“Regressive property taxes cannot be attributed simply to seniors with relatively low incomes living in relatively expensive houses. In fact, municipalities where lower-income non-seniors have the heavier tax burden far exceed those where the reverse is true.*

*“Residential property is taxed strictly as a function of its assessed value. However, because income inequality is far greater than inequality in property values, lower-income homeowners end up spending a relatively large proportion of their income on property tax.”<sup>15</sup>*

**Figure 1 - Calgary 2008 Operating Revenues (millions)<sup>16</sup>**



15 B. Palmeta and I. Macredie, “Property Taxes Relative to Income” (Statistics Canada, March 2005 Perspectives), p. 18, <http://www.statcan.gc.ca/pub/75-001-x/10305/7796-eng.pdf>. While it doesn’t appear to be taking place in Canada, property taxes in theory could be made progressive-e.g. N.C. Chin, “A more nuanced, fairer property tax” (Singapore News, February 22, 2010), <http://www.channelnewsasia.com/stories/singaporelocalnews/view/1039040/1.html>; C. Hsu and P.L.C Siong, “Taiwan Minister: Progressive Property Tax Needs Further Study” (Dow Jones Newswires, March 29, 2010), <http://www.foxbusiness.com/story/markets/industries/real-estate/taiwan-minister-progressive-property-tax-needs-study/>.

16 “The City of Calgary 2008 Annual Report, for the Year Ended December 31, 2008,” Consolidated Statement of Financial Position, p. 53 [http://www.calgary.ca/docgallery/bu/finance/reports/2008/annual\\_report\\_2008.pdf](http://www.calgary.ca/docgallery/bu/finance/reports/2008/annual_report_2008.pdf).

## Taxes, yes. Property taxes, no

Edmontonians and Calgarians differ on many things, but it turns out that municipal taxes are one of the areas where they do agree.

When asked how to balance the municipal budget, Edmontonians strongly prefer tax increases over cuts to services. However, property taxes are the least supported option for generating those additional revenues.<sup>17</sup>

Ditto Calgarians, according to a 2009 Ipsos Reid survey; the majority want taxes increased or maintained, not cut, and don't prefer property tax increases.<sup>18</sup> The imagineCALGARY plan also noted the need to diversify away from reliance on property taxes, and it set a target of reducing the City's dependence on property taxes to no more than 25 per cent of revenues by 2036. It said the City should develop a "broader palette of progressive taxation tools" to raise revenues and maximize the benefits of royalties and fees generated from non-renewable resources.<sup>19</sup>

Canadian municipalities, Calgary included, also rely on grants, revenue sharing and other funds from higher levels of government. Taxing at a higher level of government is an important mechanism for ensuring equality in services regardless of location and local incomes—a cornerstone of Canadian fiscal and social policy. It also helps prevent harmful tax competition: the possibility of municipalities engaging in a mutually destructive "race to the bottom" in tax rates in an attempt to attract businesses away from one another.

Cities are still recovering from the 1990s, when provincial governments slashed spending and transfers, retreated from traditional social support programs and downloaded responsibilities to communities, often without providing funding.

*"While the social, cultural and economic pressures facing municipalities vary, they are all filling gaps in the social safety net created by the retreat of federal and provincial governments.*

*"In tackling these challenges, municipal governments are taking over a share of social-service costs once borne by federal and provincial governments but without additional resources, and funding them primarily through a regressive fiscal tool: the property tax."*

—Federation of Canadian Municipalities<sup>20</sup>

- 17 Survey results in City of Edmonton "2010 Tax Bill at a Glance," p. 10, [http://www.edmonton.ca/city\\_government/documents/2010\\_proposed\\_budget\\_budget\\_at\\_a\\_glance.pdf](http://www.edmonton.ca/city_government/documents/2010_proposed_budget_budget_at_a_glance.pdf).
- 18 See Ipsos Reid, "The City of Calgary 2009 Citizen Satisfaction Survey," op. cit.
- 19 "imagineCALGARY Plan for Long Range Urban Sustainability" op.cit. at p. 57.
- 20 See Federation of Canadian Municipalities, "Mending Canada's frayed social safety net: The role of municipal governments" (FCM, March 2010), [http://www.fcm.ca/CMFiles/QofL6En\\_Embargp1KGE-3242010-6436.pdf](http://www.fcm.ca/CMFiles/QofL6En_Embargp1KGE-3242010-6436.pdf).

Many have pointed out that higher orders of government should start re-absorbing the social spending responsibilities that cities had to pick up. Social housing, to give an example, cost Calgary \$144 million in 2008. Social development cost another \$51 million.<sup>21</sup> These are redistribution programs that should be financed out of (progressive) income taxation.

Payments for some facilities and services within the boundaries of a city should be covered by the province, and it would be in the interests of Calgarians to receive a greater share of provincial outlays.

This said, there are several drawbacks to relying on provincial money for future growth. First, provincial grants often cannot be allocated to day-to-day operational spending priorities by municipalities; they are aimed at specific capital projects. Frequently these are “pet” projects that provide ribbon-cutting photo-ops for ministers and governing party caucus members, and they don’t always coincide with municipal infrastructure priorities.

Second, these pet-project grants tend to be conditional on matching funds from the municipality, which results in municipal money being drawn away from longstanding municipal priorities—both capital and operational.

Third, transfers from one level of government to another separate the revenue-raising and spending functions, thereby reducing transparency and public accountability for tax dollars raised.<sup>22</sup>

Finally, and most importantly, revenues from other governments are not secure. When those governments are focused on addressing deficits, transfers are unlikely to grow at the same rate as municipal spending needs. Existing funding commitments might be delayed, cut or even eliminated entirely.<sup>23</sup> The Alberta Urban Municipalities Association—like its federal and provincial counterparts—has lobbied for increased transfers from higher levels of government for many years. Unless a truly innovative lobbying strategy is adopted or the economy heats up for a long period of time, those efforts will likely see limited results.

So hiking property taxes and seeking increased transfers from higher levels of government have some downsides, and the latter is unlikely to succeed in the near future. What about other options?

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21 “The City of Calgary 2008 Annual Report, for the Year Ended December 31, 2008,” Consolidated Statement of Financial Position, p. 52, [http://www.calgary.ca/docgallery/bu/finance/reports/2008/annual\\_report\\_2008.pdf](http://www.calgary.ca/docgallery/bu/finance/reports/2008/annual_report_2008.pdf).

22 E. Slack, “Provincial-Local Fiscal Transfers in Canada: Provincial Control Trumps Local Accountability” (Institute on Municipal Finance and Governance, University of Toronto, September 2009), p. 26, <http://www.utoronto.ca/mcis/imfg/ArticlesPapersPublications/Slack-ProvincialLocal%20Fiscal%20Transfers%20in%20Canada-Copenhagen2009.pdf>.

23 E.g. J. Markusoff, “Calgary girds for funding cutback: Provincial move could force project delays” (Calgary Herald, January 25, 2010), <http://www.edmontonjournal.com/business/Increase+retirement+benefits+Canadians+Sturdy/2261800/Calgary+girds+funding+cutback/2480698/story.html?id=2480698>.

### ***Panaceas and free lunches: P3s and privatization***

In recent decades, an entire industry has sprung up on the promise of free lunches.

The sales pitches vary in the details, but at their core they all suggest that corporations are going to kick in for public facilities or services. For instance, the pitch might be that if we enter into a P3 to build a recreation facility, we can get corporations to cover the construction costs or accept the risks. Or if we privatize a service like waste collection, the cost to the public will drop.

That's the essence of the pitch. However, the reality is more commonsensical: there is no free lunch. Privatization and P3s are not the panaceas they are sometimes claimed to be by their boosters—the corporations involved and their well-funded representatives. This section takes a second look at some of those claims.

### **Who pays? Citizens**

The first claim of P3s is that the public will benefit from access to “private sector capital” to finance public projects.

Certainly, the construction of a public facility can be financed by the government or by the private sector in a P3 arrangement. However, that's just the up-front money. And like all up-front money, it has to be paid back.

So who is going to pay it back? Wherever the up-front money comes from, it is the citizens who are going to pay it back.

Corporations aren't about to hand over cash or any other asset for nothing. Shareholders would fire and sue the directors if they did. Corporations will need to be paid back in full, with the addition of a profit—one that is higher than the profits from the next best possible investment. So for financing the construction, the corporation involved in a P3 will require an agreement that puts the City on the hook for years of payments. Those annual payments will ultimately be covered by citizens.

*“Ultimately, [P3s] are entirely financed by government and/or user charges.”<sup>24</sup>*

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24 D. Whitfield, “Global Auction of Public Assets” (Spokesman Books, Nottingham: January 2010), <http://www.european-services-strategy.org.uk/global-auction-of-public-assets/>.

So advocates like to make another claim—that P3s and privatization reduce labour costs. As discussed below (see “Wider Employment Benefits of Public Investment”) reducing labour costs by firing municipal workers or cutting their salaries destroys jobs and reduces economic activity across the entire economy, including in the private sector. So really, some of those cost “savings” are actually offloading costs onto families, communities, the private sector and the economy overall. They aren’t so much a savings as a redistribution of costs.

Advocates also argue that P3s and privatization bring economies of scale and know-how. This may be valid in a smaller town, but only if the firm involved has both large-scale and more know-how and actually brings both of them to the project or service in question. If it has neither, or if it lets a smaller subsidiary or branch office manage the project or service with little involvement from the main body of the firm—or if it subcontracts it out entirely—then there may be little or no economies of scale or know-how applied. Certainly, the profit motive provides an incentive to scale down its efforts once a P3 or privatization contract is signed. Moreover, a large City like Calgary already has significant know-how and economies of scale—more than many firms.

### **ENMAX: privatize the goose that lays the golden eggs?**

ENMAX, the utility owned by the City of Calgary, continues to provide large financial returns to Calgarians. After a record revenue year in 2008, with profits of \$181 million,<sup>25</sup> ENMAX’s profit in 2009 rose to \$206 million. Of that, \$55 million will be paid to the City of Calgary as shareholder. For 2010, this dividend is scheduled to rise to \$62 million.<sup>26</sup>

There have been numerous campaigns to privatize ENMAX and they all have failed. Following the pattern of EPCOR in Edmonton,<sup>27</sup> these campaigns are accompanied by “research” reports that suggest ENMAX’s financial future is not so bright. For one campaign, “outside consultants reported...that Enmax has reached its peak.”<sup>28</sup> That was in 2001, before the record revenues and steeply rising profits and dividends.

Another report advocating for privatization called ENMAX a “risky” asset and said the City should sell ENMAX Energy

25 “Alderman calls for bigger Enmax take” (CTV News, March 20, 2009), [http://calgary.ctv.ca/servlet/an/local/CTVNews/20090320/CGY\\_enmax\\_profits\\_090320/20090320/Human%20Target](http://calgary.ctv.ca/servlet/an/local/CTVNews/20090320/CGY_enmax_profits_090320/20090320/Human%20Target).

26 “Enmax announces excellent 2009 financial results” (Enmax, March 18, 2010), [http://www.enmax.com/Corporation/Media+Room/Current+News+Releases/06\\_2009Financials.htm](http://www.enmax.com/Corporation/Media+Room/Current+News+Releases/06_2009Financials.htm).

27 D. Gibson, “EPCOR: A Study of Ownership, Accountability and the Public Interest.”

28 S. Wilton and G. Robertson, “City puts ENMAX up for sale” (Calgary Herald, July 25, 2001), available at [http://www.iasa.ca/ED\\_news\\_CalgaryHerald/CalgaryHerald22.html](http://www.iasa.ca/ED_news_CalgaryHerald/CalgaryHerald22.html).

(the electricity supply part of ENMAX) and invest the proceeds.<sup>29</sup> That was in 2006, not long before global equities markets demonstrated again that investing in them is very risky indeed. This report, of course, did not analyze the riskiness of that investment market.

In 2002, City Council voted 13-2 to reject privatization.<sup>30</sup> It is only a matter of time before the next campaign.<sup>31</sup>

Advocates also like to claim that P3s and privatization bring a cost-reducing incentive. While it is true that the profit imperative makes a corporate board or a CEO look for ways to reduce costs (profit = revenue minus costs), it is less clear that this incentive has the same force lower down the corporate bureaucracy. Many front-line corporate employees just want to hang on to their jobs. And some corporate middle managers have an incentive to avoid cutting costs—their future budgets may be cut if they do so. As for promotions for squeezing more results from the same dollar, these incentives can exist in both the private and public sectors. A bigger concern is that cost cutting—in an environment where profit is the sole overarching goal—may take place on the back of services, safety or the environment.

*“[S]ignificant service contract requirements which impact student health and safety are not being completed, such as child abuse registry and criminal record checks, and fire safety inspections”*

*- Nova Scotia Auditor General, Review of School P3s<sup>32</sup>*

Enthusiastic claims about P3 savings often are not substantiated. The Alberta government said that recent P3 school construction cost \$581 million, but it turned out that figure did not include interest or maintenance costs over 30 years, which added more than \$400 million to the total cost.<sup>33</sup> Furthermore, the Auditor General noted the province had not provided a sensitivity analysis, which is normally used to determine the impact that uncertainty about assumptions could have on the cost of alternatives. The Auditor General report noted that sensitivity analysis “should be provided where changes in significant assumptions may impact the decision.” The report noted the P3 project team “used assumptions with significant uncertainty” and pointed out that “failure to validate key cost assumptions may result in the development of inaccurate cost comparisons.”<sup>34</sup>

- 29 A. Hollis, “The City of Calgary’s Ownership of Enmax Energy Corporation: Value at Risk” (Institute for Advance [sic] Policy Research, October 2006), <http://www.ucalgary.ca/iaprfiles/technicalpapers/iapr-tp-06010.pdf>.
- 30 C. Derworiz, “Sell part of Enmax, U of C study suggests” (Calgary Herald, November 1, 2006), available at [http://www.aldermandiane.ca/documents/Herald-Nov1SellPartofEnmaxUofCStudySuggests\\_000.pdf](http://www.aldermandiane.ca/documents/Herald-Nov1SellPartofEnmaxUofCStudySuggests_000.pdf).
- 31 A similar campaign is being waged in Toronto. See T. Sanger and J. Stanford, “Selling off our public assets makes no sense for Toronto: Many of them generate stable flows of revenue that the city will lose in these one-shot deals” (Toronto Star, April 6, 2010), <http://www.thestar.com/opinion/article/790643--selling-off-our-public-assets-makes-no-sense-for-toronto>.
- 32 “Report of the Auditor General, Ch. 3 Education: Contract Management of Public-Private Partnership Schools” (Nova Scotia Auditor General, February 2010), p.30, <http://www.oag-ns.ca/feb2010/full0210.pdf>.
- 33 S. McGinnis, “Alberta announces builder for next round of P3 schools” (Calgary Herald, April 22, 2010) <http://www.calgaryherald.com/news/Alberta+announces+builder+next+round+schools/2938605/story.html>.
- 34 “Report of the Auditor General of Alberta” (April 2010), p. 24, <http://www.oag.ab.ca/files/oag/OAGApr2010report.pdf>.

Nova Scotia's Auditor General also has raised serious issues about the costs of using P3s to build schools. In one arrangement, the Department of Education was paying private sector developers to perform services, and the developers then subcontracted the services to the regional school boards at a lower rate. The Auditor General determined that this profit stream would cost the public \$52 million over 20 years.<sup>35</sup>

Advocates also claim that risks can be transferred to the private sector with P3s. The reality is that it depends on the contract, and it is hard to assess whether it is the case with a particular P3 project, as the contracts are generally hidden from the public (thus also reducing transparency and accountability). Advocates claim this secrecy is due to the need for "commercial confidentiality," not because they fear public scrutiny of these deals. However, regardless of the claims of advocates or the provisions of secret contracts, when a P3 fails, the public sector is ultimately left holding the bag for delivery of services. P3s often include a guaranteed level of profit for the corporation, no matter the cost to the public. The bottom line is that no corporation is going to absorb risk without being compensated for it; if the risk is transferred to a corporation, the price of a P3 will go up accordingly. There is no free lunch here.

### Added costs of P3s and privatization

So, we have seen that the payments for public facilities and services will be made by citizens either way; corporations aren't about to step in and foot the bill for us. What will the bill be? The advocates claim it's all about cost savings. The reality is that private sector involvement introduces a range of new and higher costs.

First, there is the need to pay off shareholders. Business corporations exist in order to make shareholders wealthier. So profits get skimmed off the top; instead of paying for facilities or services for citizens, a percentage is handed over to the corporate shareholders.

Many firms that get involved in P3s or privatization will be owned by shareholders outside of Calgary. So the profits are sent out of the city, and possibly out of Alberta and even Canada.

Next, there are the higher borrowing costs faced by corporations compared to governments. Governments generally have good credit ratings, which enable them to borrow at low interest rates. For instance, Standard and Poor's gives Calgary an AA+ credit rating.<sup>36</sup> The financial sector implosion of 2008 showed the risks of relying on

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35 "Report of the Auditor General, Ch. 3 Education: Contract Management of Public-Private Partnership Schools" (Nova Scotia Auditor General, February 2010), p. 41, <http://www.oag-nb.ca/feb2010/full0210.pdf>

36 City of Calgary, "Credit Ratings," [http://www.calgary.ca/portal/server.pt/gateway/PTARGS\\_0\\_0\\_104\\_0\\_0\\_35/http%3B/content.calgary.ca/CCA/City+Hall/Business+Units/Finance+and+Supply/Archive/Economy+Watch/Credit+Ratings.htm](http://www.calgary.ca/portal/server.pt/gateway/PTARGS_0_0_104_0_0_35/http%3B/content.calgary.ca/CCA/City+Hall/Business+Units/Finance+and+Supply/Archive/Economy+Watch/Credit+Ratings.htm).

corporations to arrange financing; many P3s were shelved when the private sector could no longer borrow money.<sup>37</sup> Another serious risk here is that the terms of P3 arrangements are kept secret. The Alberta government has entered into more than \$2 billion worth of P3s. What happens under the terms of these secret contracts when interest rates go up?<sup>38</sup>

*“The terms of the service contracts are not adequate to ensure public interest is protected. The contracts do not address significant areas such as adequate audit access for the Province; measurable service levels for all services; monitoring compliance with contract terms, including documentation requirements; and an adequate payment adjustment system to be used for non-compliance. The lack of these significant contract terms impairs the Department’s ability to hold the developers accountable and effectively manage the contracts.”*

*- Nova Scotia Auditor General, Review of School P3s<sup>39</sup>*

Next, there are the gold-plated executive compensation packages that come with private sector corporations. Those CEO bonuses don’t come cheap, and they make public sector management pay scales look small by comparison. A generation ago, top CEOs used to make 30 to 40 times the pay of average workers; now they make 344 times as much.<sup>40</sup>

Next there are the other incidental costs of running a successful, multinational business corporation: advertising and marketing; lobbying governments; making donations to political parties; and producing contract bids, when the contracts are not sole-sourced. When doing business in some countries, the cost of bribes needs to be factored in. And even if those bribes are paid in Germany or the US,<sup>41</sup> for a multinational company the cost can end up being spread to other countries (including Canada).

Another cost of P3s and privatization is the resulting loss of capacity in the public sector. When P3s are used or public services are privatized, the ability of the public sector to manage such things in the future is diminished. Furthermore, the ability to even assess the value of the services or construction costs is diminished due to “information asymmetry”—the corporations have the information, which compromises the public sector’s bargaining position.

A further cost is the loss of financial transparency in government. When government finances construction of a facility, it incurs debt and pays it back over time. That debt shows up clearly on the liabilities side of the balance sheet. However, if the financing is done by a

37 For this and other reasons, “[g]lobally, nearly 1,000 PPP and privatisation projects, valued at over US\$500bn, have been terminated or radically reduced,” D. Whitfield, “Profiteering from public-private partnerships” (Guardian, December 10, 2009), <http://www.guardianpublic.co.uk/ppp-projects-investment-funds>.

38 D. Braid, “Be wary, very wary of savings promised with P3,” (Calgary Herald, April 24, 2010), <http://www.calgaryherald.com/Braid+very+wary+with/savings+promised+with/2947017/story.html>.

39 “Report of the Auditor General, Ch. 3 Education: Contract Management of Public-Private Partnership Schools” op.cit. at p. 37.

40 This is a US study, and many head offices of multinational P3 corporations are in the US. S. Anderson and S. Pizzigati, “Workers Need Added Clout to Close the Pay Gap with CEOs” (Institute for Policy Studies, September 1, 2008), <http://www.ips-dc.org/articles/658>.

41 N. Avelling, “Karlheinz Schreiber in German jail” (Toronto Star, August 3, 2009), <http://www.thestar.com/article/675498>. See also D. Hall, “More public rescues for more private finance failures- a critique of EC Communication on PPPs” (PSIRU, March 2010), p. 14, [http://www.epsu.org/IMG/pdf/2010-03-PPPs\\_FINAL.pdf](http://www.epsu.org/IMG/pdf/2010-03-PPPs_FINAL.pdf).

corporation, the government might not show the liability in the same way. Of course, taxpayers will still be on the hook to make payments to the corporation for 20, 30 or 40 years. That's how Enron hid its debt-by farming it out to offshore corporations. And when it comes to election time, a seemingly healthy balance sheet can sometimes buy votes.

*"[I]t cannot be taken for granted that PPPs are more efficient than public investment and government supply of services. One particular concern is that PPPs can be used mainly to bypass spending controls, and to move public investment off budget and debt off the government balance sheet, while the government still bears most of the risk involved and faces potentially large fiscal costs."*

- *International Monetary Fund Report on Public-Private Partnerships*<sup>42</sup>

*"[T]hey wanted to manipulate the numbers at that time in order to avoid putting these schools on the books of the province and incurring debt. So they wanted to make sure that it fit the technical accounting rules to be operating leases and not capital leases."*

- *Testimony of the Auditor General of Nova Scotia*<sup>43</sup>

In a nutshell, there are many costs that the private sector racks up that don't exist when the public sector tackles a project or provides a service.<sup>44</sup> And those costs will be passed along to citizens.

It is perhaps because of these added P3 costs that the PPP Canada Fund was created—with an initial endowment of \$1.2 billion in public money. PPP Canada will provide up to a quarter of the costs of P3 projects.<sup>45</sup> The fact that P3 projects would require such significant public subsidies in order to be attractive to governments suggests that the business case for P3s is marginal, at best.

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42 T. Ter-Minassian, "Public-Private Partnerships" (International Monetary Fund, Fiscal Affairs Department, March 12, 2004), p. 3, <http://www.imf.org/external/np/fad/2004/pifp/eng/031204.pdf>.

43 Hansard, Nova Scotia House of Assembly, Committee on Public Accounts (February 3, 2010), p. 20, [http://www.gov.ns.ca/legislature/hansard/comm/pa/pa\\_2010feb03.htm](http://www.gov.ns.ca/legislature/hansard/comm/pa/pa_2010feb03.htm).

44 For an international analysis of P3 costs, publicly funded bailouts and the claims made on their behalf, see D. Hall, "More public rescues for more private finance failures—a critique of EC Communication on PPPs" (PSIRU, March 2010), [http://www.epsu.org/IMG/pdf/2010-03-PPPs\\_FINAL.pdf](http://www.epsu.org/IMG/pdf/2010-03-PPPs_FINAL.pdf).

45 PPP Canada, FAQs <http://www.p3canada.ca/faq.php>. For a Canadian analysis of some of the claims for P3s, see T. Sanger, "The Conference Board on P3s: Biased and Superficial" (CUPE, Feb 2010).

### ***New revenue sources that reduce costs***

Clearly, transfers and grants have some strings attached, and cannot be relied upon. Property taxes are quite unpopular—many would say deservedly so. Privatization and P3s carry a lot of added costs.

Another course worth exploring is the development of alternative local revenue streams. Expanding other slices of the revenue pie would provide needed revenues, and it could even help to offset regressive property taxes.

### **Reducing externality costs**

If the City is going to look into a wider range of revenue sources—as suggested by Calgarians—it needs to consider the effect of collecting those revenues. Whether as charges, taxes or user fees, the collection of public revenues can have positive effects for an economy and for people. These positive effects are not only in the public services and facilities that those revenues make possible. The charges, taxes or user fees themselves can have positive effects.

It is widely understood that when the price of a thing goes up, people and firms will want to consume less, and so less will be produced. And when the price goes down, they will want to consume more, and so more will be produced.

There are some things that citizens generally want more of. Examples often include recreational space, education, quality health care, transit, recycling, employment and community spirit. (If this list sounds familiar, it should; it largely corresponds to the things Calgarians identified as priorities in the imagineCALGARY process.)

For other things, citizens generally want less. Examples include environmental degradation, poverty and homelessness, addictions (drug, alcohol, gambling), traffic congestion and excessive energy and water consumption. These are the things that are commonly associated with negative externalities (see below, Market Failure and Externalities).

To connect the dots, if the City is going to implement new charges, taxes and user fees, or raise some of the existing ones, it should do so in relation to things we want less of.

## **Market failure and externalities**

In an ideal market transaction, the full costs and benefits of producing a good or service are included in the price.

However, the market is often less than ideal.

For some goods and services, the market price omits the environmental costs. The classic example is an industrial facility that emits pollution, causing health problems to people nearby. The costs of ill health are not included in the price of the goods produced at the facility. In other words, such costs are “externalized” from the market transaction. Economists call these costs “externalities.”

Such negative externalities are a type of market failure, and market failures create economic inefficiency and reduce wealth. They also result in excessive consumption; because some of the costs are externalized, the good or service has an artificially low price. Thus it is going to be over-consumed and over-produced.

Pollution is an example of a negative externality. It can be addressed by government increasing the price of the transaction—effectively including the externalized cost in the market transaction via regulation, or by charges, taxes or user fees. This financial incentive encourages the producer to clean up the externality.

Other externalities are positive. Education and health care provide benefits not only to the individuals receiving them, but also to others, e.g. employers. For such “public goods,” the appropriate pricing adjustment is a subsidy. This is why public education and health care make good economic sense.

So before starting to look for new revenue sources, the City should first conduct an inventory of what Calgarians want more of and what they want less of. With this in hand, it becomes fairly clear where revenues can and should be raised—and where higher subsidies are appropriate.

<b>Negative externalities (use charges, taxes, user fees)</b>	<b>Positive externalities (use subsidies)</b>
Water wastage	Transit
Energy wastage	Education
Traffic congestion	Community facilities and parks
Derelict land and urban sprawl	Urban revitalization
Etc.	Etc.

*“If society as a whole benefits from an activity, then society as a whole should pay the proportion of the costs of that activity that reflects the societal benefit. The City collects money from citizens through the tax system and is able to provide subsidies to the activities which benefit society at large.*

*“... The most equitable means of remedying a social cost is to require individuals to pay for the negative impacts of the activity. This is often done through selective taxation and regulation.”*

*- City of Calgary<sup>46</sup>*

### Reducing financial costs

In addition to reducing externalities, a well-designed revenue source can also reduce financial costs to the City. By reducing demand for a thing (e.g. water or road space), a charge, tax or user fee reduces excessive consumption and waste. This, in turn, reduces the amount of money that the City needs to spend on the related infrastructure, including construction, maintenance, repairs, decommissioning and replacement.

These costs can be very high. Between capital and operations, the City of Calgary spends about \$900 million a year on water and roads.<sup>47</sup> Saving just 10 to 20 per cent of that cost would free up \$90 million to \$180 million for priority public services and facilities—every year.

While raising revenues from facilities and services can reduce consumption and both capital and operating costs to the City, the precision and benefits of such a system can be taken a step further, by using “smart pricing.”

46 City of Calgary, “User Fees and Subsidies Policy,” Policy FCS013 (April 28 2008), p. 3, [http://www.calgary.ca/docgallery/bu/cityclerks/council\\_policies/fcs013.pdf](http://www.calgary.ca/docgallery/bu/cityclerks/council_policies/fcs013.pdf). Unfortunately, the Policy contains a number of contradictory statements and it is unclear whether this statement prevails and guides actual policy.

47 In 2008, \$382 million for roads and \$538 million on water. An additional \$223 million was spent on public works, which includes infrastructure services and facilities. “The City of Calgary 2008 Annual Report, for the Year Ended December 31, 2008,” Consolidated Statement of Financial Activities, p. 58, [http://www.calgary.ca/docgallery/bu/finance/reports/2008/annual\\_report\\_2008.pdf](http://www.calgary.ca/docgallery/bu/finance/reports/2008/annual_report_2008.pdf).

The required delivery capacity of utilities is determined by “peak load.” The scale of water treatment facilities, electrical generation capacity and road space required is set by the maximum amount of water, electricity and road demand, which varies by day and by hour.

Prices also can be varied by day and by hour. They can be higher at times of peak load, thereby encouraging firms and individuals to consume more of the public services and facilities during non-peak hours.<sup>48</sup> With peak loads reduced, capacity expansions can be deferred or even cancelled, thus saving major capital investment costs.

### **A variety of revenue sources**

There are a number of changes that could be made to Calgary’s revenue mix to reduce environmental, social and economic costs and to boost revenues. They include a community infrastructure levy or tax, hotel tax, property transfer tax, fuel tax, vehicle registration surtax, parking tax and waste disposal user fees. These and others are discussed in the City of Calgary’s Financing Growth Strategy.<sup>49</sup>

The point is not to raise taxes in every possible area, but to shift the mix of taxes so as to lower the price of the “goods” and increase the cost of the “bads.”

Certainly, there are few who would argue that the City’s current mix of taxes is optimal. Changing the mix can yield environmental, social and economic benefits, as well as diversifying City revenue streams.

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48 E.g. see Climate Change Central, “Smart Meters Could Help Reduce Electricity Use,” <http://www.climatechangecentral.com/publications/c3-views/january-2009/smart-meters-could-help-reduce-electricity-use>.

49 City of Calgary, “Financing Growth Strategy: Sustainable Growth. Equitable Financing,” (January 2005) [http://www.calgary.ca/docgallery/bu/planning/pdf/2005\\_1077\\_financing\\_growth.pdf](http://www.calgary.ca/docgallery/bu/planning/pdf/2005_1077_financing_growth.pdf).

50 At 10 per cent of income, the flat tax paid rises with income. At lower levels of income, the rate is zero.

### **Progressive and regressive solutions**

For some, the very mention of charges or user fees brings back unpleasant memories of the 1990s, when many governments began to slap charges and user fees on important public goods. As noted above, public goods instead should be subsidized because of their positive externalities.

Furthermore, some of these so-called user fees were actually more akin to a head tax—a flat amount paid per person, per year, regardless of consumption or income. A head tax is far more regressive than Alberta’s “flat tax” on personal incomes;<sup>50</sup> indeed, it is the most

regressive form of taxation. An example of such a head tax was Alberta's hated healthcare premium, which the government wisely eliminated in 2009.

Fortunately, however, charges and user fee systems don't need to be regressive. They can be designed to be progressive in relation to income, wealth (value of property) and/or consumption. This would help to implement the City's Fair Calgary Policy,<sup>51</sup> and tackle the growing challenge of income disparity in Calgary. With the exception of Vancouver, Calgary is growing more unequal faster than any other city in Canada.<sup>52</sup>

As an example of careful instrument design, the price for using a utility (electricity or water) can be structured so that the price per unit consumed is low for moderate amounts and high at higher levels of consumption (where there is even more incentive needed for conservation). This is termed the "increasing block billing" structure and it is growing in popularity.<sup>53</sup> It provides an incentive to reduce wastage and excessive consumption.

The price paid per unit can be reduced further—even to zero—for low usage levels. This is termed a "lifeline" rate structure and is aimed at ensuring that lower income citizens can and do use the utilities. (It is important that everyone use water for sanitation and food preparation).

Prices also can be adjusted directly for income (e.g. to rebate a portion of the costs for lower-income citizens) or for the value or size of a property, or for the number of people in a residence in order to encourage densification.

Rebating based on income sometimes can be administratively expensive and even demeaning to recipients, depending on the arrangements. Another option is to offset the cost by providing universal benefits and good social programs, financed by the revenues collected.

51 City of Calgary, Policy CSPS034, [http://www.calgary.ca/docgallery/bu/cityclerks/council\\_policies/csp034.pdf](http://www.calgary.ca/docgallery/bu/cityclerks/council_policies/csp034.pdf).

52 Federation of Canadian Municipalities, "Mending Canada's frayed social safety net: The role of municipal governments" (FCM, March 24, 2010), p.10, [http://www.fcm.ca/CMFiles/QofL6En\\_Embargp1KGE-3242010-6436.pdf](http://www.fcm.ca/CMFiles/QofL6En_Embargp1KGE-3242010-6436.pdf). See also G. Steward, "Dashed Dreams, New Realities: Calgarians Talk Frankly about the Impact of the Economic Downturn" (Sheldon Chumir Foundation, 2009), [http://www.chumirethicsfoundation.ca/files/pdf/Dashed\\_Dreams\\_Report\\_091509-lowres.pdf](http://www.chumirethicsfoundation.ca/files/pdf/Dashed_Dreams_Report_091509-lowres.pdf).

53 Between 1991 and 2004, this rate structure for water rose from three per cent to 23 per cent of residential ratepayers—the fastest increase of any structure. Environment Canada, "2008 Municipal Water Pricing Report," [http://www.ec.gc.ca/WATER/en/manage/data/e\\_MUP2008.htm](http://www.ec.gc.ca/WATER/en/manage/data/e_MUP2008.htm), accessed November 30, 2008.

## Free roads and the Calgary policy on user fees and subsidies

The first principle in Calgary City Council’s User Fees and Subsidies Policy<sup>54</sup> is the Benefits Principle—that “those who receive benefits from a municipally provided good or service should pay for that good or service according to the level of value of the benefit received.”

It is difficult to see how this policy has been applied in respect to roads. Currently, road use in Calgary is priced at zero. In contrast, many cities worldwide,<sup>55</sup> including in North America, employ road tolls.

Often the assertion is made that fuel taxes pay for roads. The reality is that they don’t. Fuel taxes generally fail to cover even the financial costs of building and maintaining roads. Fuel taxes, even when added to other fees and charges related to motoring, only cover about 60 to 70 per cent of those costs. The remainder is covered by subsidies from other tax sources.<sup>56</sup>

There is a further layer of costs that fuel taxes don’t even begin to cover. These are the environmental, social and economic costs of excessive motoring. Traffic congestion hinders economic productivity, smog and collisions kill and send others to hospital, and greenhouse gas emissions contribute to climate change. Sprawl, exacerbated by this road-use subsidy, eats up farmland, hollows out established neighbourhoods and creates long-term infrastructure maintenance and replacement liabilities, as well as locking in a pattern of automobile dependency.

These are very real costs, and someone is paying them. But they aren’t being paid by the “marginal user”—the person who decides to drive on a given road at a given time of day. These costs are thus termed externalized costs, or externalities (see above, Market Failure and Externalities). Certainly the service provided by roads is not being paid “according to the level of value of the benefit received.”

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54 City of Calgary, “User Fees and Subsidies Policy,” Policy FCS013 (April 28, 2008), p.2, [http://www.calgary.ca/docgallery/bu/cityclerks/council\\_policies/fcs013.pdf](http://www.calgary.ca/docgallery/bu/cityclerks/council_policies/fcs013.pdf).

55 See, for examples, “Road Pricing: Congestion Pricing, Value Pricing, Toll Roads and HOT Lanes-Case Studies” (Victoria Transport Policy Institute, Updated May 9, 2010), <http://www.vtpi.org/tdm/tdm35.htm>.

56 C. Vander Ploeg, “Delivering the Goods: Infrastructure and Alternative Revenue Sources for the City of Edmonton,” (Canada West Foundation, June 2008), p. 31, [http://www.cwf.ca/V2/files/Delivering\\_goods.pdf](http://www.cwf.ca/V2/files/Delivering_goods.pdf).

It is worth emphasizing that municipal facilities and services do have real costs (financial and ecological) and that we do pay them, one way or another. The real question is how we distribute those payments. The main municipal alternative to charges and user fees is the property tax, which is regressive, as noted above. Transfers from the Alberta government, apart from being unreliable, are partly financed by a flat personal income tax, unlike progressive income taxes elsewhere. Charges and user fees can be structured in a progressive manner, and can provide reliable sources of operational funding for important public services and facilities.

*“[T]he current system...amounts to a ‘subsidy for larger households that use a lot of electricity and water and generate more waste’ .... These subsidies redistribute income, but in a manner that provides more support for the rich than for the poor.”*

*- Mintz and Roberts, “Running on Empty”<sup>57</sup>*

User fees can be designed to be regressive, neutral or progressive. There is nothing about user fees that makes them inherently regressive. Ensuring they are not regressive is just a matter of smart instrument design.

### Calgary’s waste management charge

The City of Calgary has instituted a waste management charge to provide funding for capital projects and upgrades at the City’s landfills.

Across Canada, the United States, and elsewhere, cities are exploring methods to pay for solid waste collection and disposal. Many are dropping property taxes and adopting pay-as-you-throw systems, where householders pay on a bag-per-week basis (often with the first bag being free). Such systems provide an incentive to reduce excessive waste.<sup>58</sup>

Calgary’s waste management charge, in contrast, is levied at a flat rate of \$4.20 per month per household, regardless of volume of waste produced. This structure of charge provides no incentive to reduce household waste generation through recycling, home composting or buying fewer items with excessive packaging material. Once again, it is hard to see how this charge relates to Principle No. 1 of City Council’s

57 J. Mintz and T. Roberts, “Running on Empty: A Proposal to Improve City Finances” (C.D. Howe Institute, February 2006), p. 11, [http://www.cdhowe.org/pdf/commentary\\_226.pdf](http://www.cdhowe.org/pdf/commentary_226.pdf), December 10, 2008.

58 See M. Kelleher, J. Robins and J. Dixie, “Taking Out the Trash: How To Allocate the Costs Fairly” (C.D. Howe Institute, July 2005), [http://www.cdhowe.org/pdf/commentary\\_213.pdf](http://www.cdhowe.org/pdf/commentary_213.pdf).

User Fees and Subsidies Policy, which holds that those who receive benefits from a municipally provided good or service should pay for that good or service “according to the level of value of the benefit received.”<sup>59</sup>

Furthermore, in terms of its distributional consequences, this charge is similar to property taxes, except that it does not take into account the value of the property. Thus, it is probably even more regressive than a property tax.

Finally, the size of the charge seems to be set to cover only the financial costs of waste management and not the environmental costs. Even a landfill managed in accordance with provincial regulations is going to have some environmental costs.

Fortunately, it appears that the City will be considering, at some point in the future, moving toward a charge based on the amount of garbage produced.<sup>60</sup>

As we have seen, Calgarians are willing to pay for good public services and facilities. This may be related to the fact that most Calgarians can afford them. Calgary has Canada’s highest per-capita average personal income, and has had the highest average annual growth in per-capita personal income over the last ten years. Calgary families also had, on average, more than double the financial assets of the average Canadian family.<sup>61</sup>

It is important to note that not all Calgarians are thriving financially. As noted above, Calgary is growing increasingly unequal and doing so faster than almost any other city in Canada. On the other hand, those toward the bottom of the income scale could stand to benefit the most by a policy shift toward excellent public services and facilities, such as social housing and social development programs.

Although Calgary was hit by the recession, as were other major Canadian cities, it is headed back to leading in economic growth. In 2011, it is projected to have the highest GDP growth among the major cities, at 4.4 per cent.<sup>62</sup>

So there appears to be policy and economic promise for expanding and diversifying revenue sources. Does the City have the capacity to do it?

59 City of Calgary, “User Fees and Subsidies Policy,” Policy FCS013 (April 28, 2008), p. 2, [http://www.calgary.ca/docgallery/bu/cityclerks/council\\_policies/fcs013.pdf](http://www.calgary.ca/docgallery/bu/cityclerks/council_policies/fcs013.pdf).

60 City of Calgary, “Waste Management Charge,” [http://www.calgary.ca/portal/server.pt/gateway/PTARGS\\_0\\_0\\_784\\_203\\_0\\_43/http%3B/content.calgary.ca/CCA/City+Hall/Business+Units/Waste+and+Recycling+Services/Waste+Management+Charge/Waste+Management+Charge.htm](http://www.calgary.ca/portal/server.pt/gateway/PTARGS_0_0_784_203_0_43/http%3B/content.calgary.ca/CCA/City+Hall/Business+Units/Waste+and+Recycling+Services/Waste+Management+Charge/Waste+Management+Charge.htm).

61 Calgary Economic Development, “Calgary Wealth: Fact Sheet” (January 2009), [http://www.calgaryeconomicdevelopment.com/files/CED\\_-\\_Calgary\\_Wealth\\_Fact\\_Sheet\\_2008.pdf](http://www.calgaryeconomicdevelopment.com/files/CED_-_Calgary_Wealth_Fact_Sheet_2008.pdf).

62 L. Schmidt, “Calgary GDP to zoom ahead in 2011” (Calgary Herald, April 8, 2010), <http://www.calgaryherald.com/business/Calgary+zoom+ahead+2011/2777036/story.html>.

## The City, the region and the province

Some municipalities may fear competition from other municipalities when considering how to raise revenues. The fear being fostered is that any thought of a tax increase will result in a massive exodus of business and citizens to low-tax havens.

Despite the hype, the reality is that people and businesses aren't likely to pack up and move as a result of taxes, especially when the associated public spending results in improved services and facilities.<sup>63</sup> There are many other factors at play in determining location preferences, including quality of life, transportation times, access to markets and amenities, etc. The parks, the vibrant downtown core, the nightlife, the walking and cycling trails, the restaurants and shops—to put it briefly, Calgary has a lot going for it.<sup>64</sup>

However, municipalities are hemmed in on the legal side. They have very limited legal powers to raise revenues. They lack independent constitutional status, being mere creatures of provincial governments. Thus they only have the revenue-raising powers that provincial governments provide them with by statute. Those powers are generally very restricted compared to municipalities in the US and other countries.

Clearly, provinces have some tight apron strings on many cities, and Calgary is no exception.

### The City of Toronto Act

While most cities chafe under the restrictions imposed by provincial governments, the City of Toronto is experiencing new-found freedom.

Toronto is one of a number of big cities to have obtained broader revenue-raising powers. The City of Toronto Act,<sup>65</sup> allows the City to broadly levy fees or charges for services it provides. In addition to traditional property tax powers, the Act allows the City to impose “direct taxes”—like a province does—with a number of exceptions. While the exceptions are significant, the general inclusion approach gives greater revenue-raising powers than the traditional approach.

63 H. Mackenzie and R. Shillington, “Canada’s Quiet Bargain: The benefits of public spending” (CCPA April 2009), [http://www.policyalternatives.ca/sites/default/files/uploads/publications/National\\_Office\\_Pubs/2009/Benefits\\_From\\_Public\\_Spending.pdf](http://www.policyalternatives.ca/sites/default/files/uploads/publications/National_Office_Pubs/2009/Benefits_From_Public_Spending.pdf).

64 This said, it might be useful for the City of Calgary to discuss this with neighbouring municipalities and reach agreements over tax rates. With its size and its control over infrastructure used by neighbouring municipalities and their residents and businesses, Calgary is in a strong negotiating position.

65 City of Toronto Act, 2006, S.O. 2006, Ch. 11, Schedule A, [http://www.e-laws.gov.on.ca/html/statutes/english/elaws\\_statutes\\_06c11\\_e.htm](http://www.e-laws.gov.on.ca/html/statutes/english/elaws_statutes_06c11_e.htm).

Early in Canada's history, it was appropriate for small (and presumably less competent) governments to be carefully controlled in their fiscal powers. For instance, only the Federal government was given the power to raise taxes indirectly; the provinces were limited to direct taxes. And cities were largely limited to property taxes.

Since then, of course, the taxation powers of both senior levels of government have effectively expanded to allow a wide range of revenue streams. However, municipal powers have remained largely restricted. For big cities, this is no longer appropriate.<sup>66</sup> Many big cities now have larger populations than their home provinces had when they joined confederation, and they are far more professionally managed. Some of the larger cities have received broader revenue-raising powers, e.g. Toronto and Vancouver.

Calgary is a big city. It would be appropriate for the provincial government to treat it as such and give it greater flexibility around its mix of revenues.

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66 For several reports and presentations on this point, see Institute on Municipal Finance and Governance, Munk Centre for International Studies, University of Toronto, <http://www.utoronto.ca/mcis/imfg/resources.htm>.

## The high return on public investment

We have seen that Calgarians want to create a better community, and also that there are creative methods to finance the needed public investments—methods that will have positive environmental and social effects.

In addition, a third level of benefits is available from such a program of public investment. Public spending provides major economic and employment benefits. Those benefits extend to the private sector and across the entire economy. Economies are, after all, networks of interactions between people; there isn't one private sector economy and a wholly separate public sector. So when a City employs people to provide public goods and services, there are spinoff benefits to others.

### ***Wider employment benefits of public investment***

Investing in public services and facilities creates many benefits to the community beyond the direct service or facility provided. The investment dollars ripple outward to create jobs and economic growth across the economy.

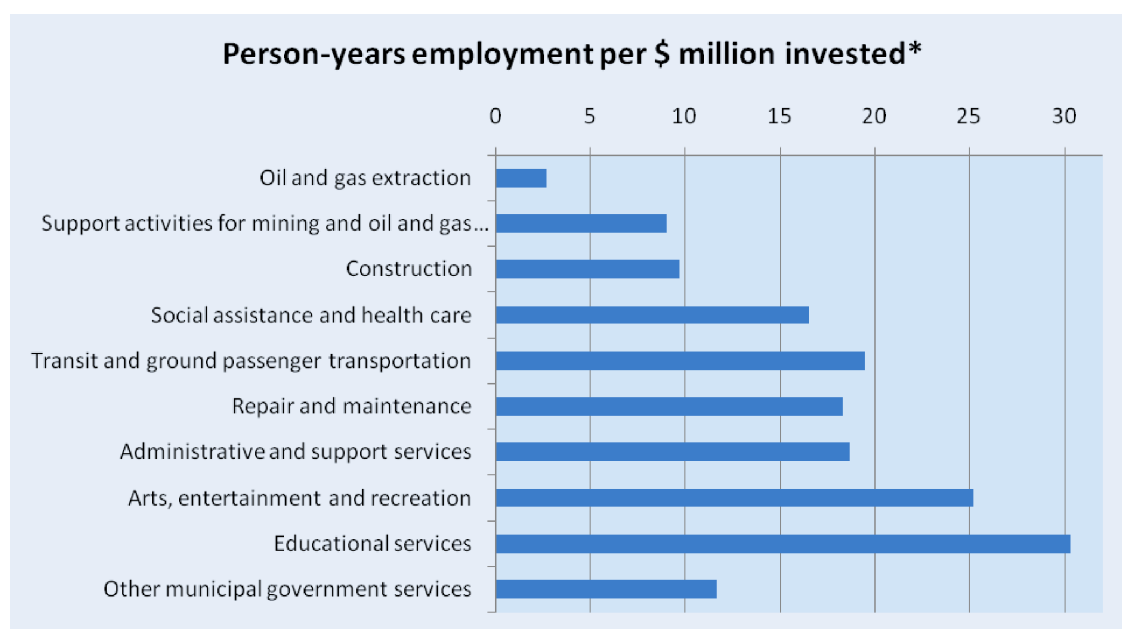
**Direct employment.** Obviously the investment in providing public goods and services generates employment for the people hired to provide them. This “direct” employment supports families and keeps them from needing employment insurance, welfare and subsidized housing, thereby maintaining stronger communities and reducing other public expenditures.

**Indirect Employment.** Investment in public services also provides “indirect” employment—jobs in the industries that are suppliers to the government, providing public goods and services. Again, those jobs support families and communities and reduce other public expenditures.

**Induced Employment.** Those people employed directly in providing public services and those employed indirectly in the supply chains then go out and spend money. This creates a third level of employment—“induced” employment—in other industries, again supporting families and communities.

This rippling outward of the benefits of public investment is termed the multiplier effect, and its strength is one of the reasons why investing in public services creates such a powerful economic stimulus. Likewise, it is why cuts to public services end up killing jobs in the private sector.<sup>67</sup>

Of course, the number of jobs created or maintained by a given level of public investment varies depending on what industry is being invested in. It turns out that municipal services provide significant bang for the buck when it comes to employment.



\* Source of data: Government of Alberta Economic Multipliers<sup>68</sup>

The top bar—the oil and gas extraction industry—represents the provincial government’s most favoured private sector recipient of public dollars. Thus it is worthwhile to take a closer look at it and use it as a point of comparison. The provincial government has poured billions of dollars of subsidies into that industry in the last two years, ostensibly in order to create jobs. Unfortunately, in terms of jobs created per dollar, that industry ranks at the bottom of the pack among the 60 industry categories in Alberta. It creates just three person-years employment per million dollars. Every other industry creates more. As a publicly funded job creation strategy, it would make more financial sense to pay workers \$300,000 per year to play golf. The second bar shows that the industry providing support to the oil and gas extraction sector creates more jobs per dollar, but still far fewer than municipal government sectors.

67 For a discussion of the job-destroying impact on the private sector of possible spending cuts at the provincial level, see Alberta Federation of Labour, “Worse Than the Recession? How government budget cuts could kill more Alberta jobs than the recession” (January 2010), <http://www.afl.org/upload/WorseThanTheRecessionWEB.pdf>.

68 Includes direct, indirect and induced employment. “Alberta Economic Multipliers 2005” (Government of Alberta, 2009).

Construction creates about 10 person-years employment per million dollars invested. Social assistance and health care create significantly higher employment, as do transit, repair and maintenance, and administration. The arts sector—often the first to be cut—creates still more jobs, at 25 person-years employment per million dollars invested. Education creates a lot of jobs—about 10 times the level of oil and gas extraction. Finally, “other” municipal government services create about 12 person-years employment per million dollars invested, significantly more than oil and gas extraction or its supporting industries.

It is important to bear in mind that the reverse is also true. When governments cut public spending, on a dollar-for-dollar basis, more people are thrown out of work. So cuts to municipal staffing levels would have a significant negative impact on the private sector: municipal layoffs kill private sector jobs.

### **Wouldn't tax cuts create more jobs?**

Some free market fundamentalists make the claim that if a government cuts taxes and services, the private sector will create new jobs. Would this make up for the jobs destroyed by public sector cuts—direct, indirect and induced?

The short answer is no.

It is correct that if a firm pays less in taxes, it has more money available to it, which it could invest in local job creation. However, it has several other options for that money. It could provide it to its shareholders, through dividends or share buybacks. It could use it to finance mergers or acquisitions of other companies. It could pay down debt. It could invest in machinery or other capital. Or it could simply put it in the bank. Not all of these activities will generate a lot of jobs locally.

Likewise, individuals won't necessarily spend the money they get from a tax cut on goods or services that create employment locally; they may pay down debt, save or spend on imports.

For these reasons, tax cuts are less effective than public spending on job creation or job maintenance. Not unexpectedly, an International Monetary Fund study of

developed economies found employment multipliers for public spending were approximately double those for tax reductions.<sup>69</sup>

So while cutting taxes might create some jobs, it might not. And in any event, it won't create or maintain as many jobs as equivalent public service cuts destroy.

### ***Wider economic benefits of public investment***

So municipal government sectors create and maintain more jobs per dollar invested. What about economic growth?

As is the case with employment, the economic impacts of investments vary across industries. And once again, comparing Alberta's benchmark industry for public job creation dollars—oil and gas extraction—we see that investment in municipal services provides significantly higher GDP growth.

Public investment creates ripples of growth across the economy. Municipal goods and services require suppliers, and municipal and supplier workers spend money that other industries turn into economic activity. As with employment, we have direct, indirect and induced degrees of economic growth.

A million dollars invested in oil and gas extraction yields only \$981,000 worth of GDP increase. For oil and gas extraction support industries, the result is little better, at \$1.016 million. In comparison, the average GDP yield per million dollars invested in the municipal sectors in the figure above is more than 20 per cent higher.<sup>70</sup>

So whether considered as job creation or overall economic stimulus, investing in excellent municipal public services makes a lot of sense. And, of course, cuts to public spending have negative consequences for the entire economy, including the private sector—both in terms of jobs and economic activity.

### ***Impacts on Calgary versus impacts elsewhere***

It is important to note that the multipliers presented above are Alberta-wide. However, spinoff employment and economic activity can take place at any number of locations. So the employment and economic benefits of investments may be generated in Calgary or elsewhere in Alberta or Canada, or in other countries altogether.

69 A. Bowen, S. Frankhauser, N. Stern and D. Zenghelis, "An outline of the case for a 'green' stimulus" (Grantham Research Institute and Centre for Climate Change Economics and Policy, February 2009), p. 6, <http://www.lse.ac.uk/collections/granthamInstitute/publications/An%20outline%20of%20the%20case%20for%20a%20%27green%27%20stimulus.pdf>.

70 22 per cent higher than for oil and gas support industries and 26 per cent higher than for oil and gas extraction itself. "Alberta Economic Multipliers 2005" (Government of Alberta, 2009).

Thus, multipliers in a city could be expected to vary from provincial-level multipliers. Generally they will be lower—both for jobs and GDP—due to “leakage.” In a nutshell, some of the indirect and induced benefits of investment will be enjoyed elsewhere.

Again, the extent of leakage varies from industry to industry. An industry that requires major capital investment in equipment that is manufactured elsewhere will generally leak more jobs and GDP than other industries. The oil and gas extraction sector comes to mind.<sup>71</sup>

Likewise, an industry that has top management offices outside of the community, or that generates value that is exported, will create relatively few local jobs and spinoff economic benefits. Again, the oil and gas extraction industry, with its heavy reliance on multinational corporations and exports, is such an industry.

On the other hand, an industry that is more labour-intensive, less capital-intensive and less reliant on imports, and that is locally directed and focused on providing local value, will tend to have less leakage. Municipal government services come to mind here.

So in examining the Alberta-wide multipliers, some caution is warranted. Generally, the positive impacts of any investment will be lower due to leakage. However, more importantly, the relative impacts in comparing industries are likely similar at the Calgary level. If anything, because of the structure of the industries, the employment and GDP advantages of investing in public services, as compared to more capital intensive and import intensive industries, will be even greater at the municipal level.

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71 E.g. G. Lamphier, “Imperial snubs Alberta workers: \$250M job goes to South Korea-and it looks like more will follow,” (Edmonton Journal, May 15, 2010), <http://www.edmontonjournal.com/business/Gary+Lamphier+Imperial+snubs+Alberta+workers/3032375/story.html>.

## Conclusions

The City of Calgary has a number of options for addressing budgetary issues over the coming years—increasing property taxes, hoping for and asking for increased provincial funding, cutting programs and services, and developing new revenue options.

What we know is that Calgarians want improvements to the City, in many areas. These preferences, in addition to the need to support Calgary’s economic and population growth, will drive spending and will require Calgary to find additional revenues.

Regressive property taxes, increased provincial transfers, and P3s and privatization are all problematic. Fortunately for City Council, Calgarians support the idea of exploring a new range of revenue sources. And fortunately for Calgarians, these sources can be designed well, so as to meet revenue needs and also have positive social, environmental and other effects.

Furthermore, the benefits that come from these investments in public services and facilities will accrue across the economy, creating jobs and economic activity in the private sector.

In a democracy, it is important to take citizen preferences seriously. Relying on old myths does a disservice to those citizens. The City has the capacity and the political room to address its financial needs honestly. If the City steers the public policy dialogue to what Calgarians actually want and to attractive ways of getting there, it could even improve voter turnout.

Calgarians are ready for a mature conversation about public services, facilities and revenues.

Is the City?





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ISBN 978-1-894949-28-6