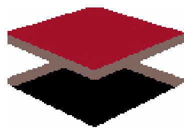
# PROVINCIAL/MUNICIPAL FISCAL RELATIONSHIPS

**A Report Prepared For**

**The Capital Region Municipalities**
**(Charlottetown, Cornwall and Stratford)**

**November 20, 2008**



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# 1.0 EXECUTIVE SUMMARY

## 1.1 Introduction

The City of Charlottetown and the Towns of Stratford and Cornwall (the Capital Region Municipalities) were incorporated in 1994 by an Act of the Legislative Assembly of the Province of Prince Edward Island which amalgamated a number of smaller communities in the region. With amalgamation Provincial grant programs were replaced by a Comprehensive Urban Services Agreement (CUSA). During the Legislative Assembly session in the winter of 2008, government through the Budget and an Act of the Legislature abandoned the tax credit system outlined in the CUSA and replaced it with a new municipal grant program. This significant change, in the view of the Capital Region Municipalities, has seriously constrained their ability to plan for and manage their communities and to provide their citizens with essential services. The Capital Region Municipalities engaged the services of MacPherson Roche Smith & Associates (MRS&A) to provide a complete understanding of the new municipal grant program and of its implications for each of the three municipalities. To assist in the study MRS&A engaged the services of Dr. Enid Slack, one of Canada's foremost experts in municipal finance. This Report provides an independent assessment of the existing situation and is intended to form the basis for urgent and meaningful discussion with the Provincial Government with respect to the new municipal grant program and related issues.

## 1.2 Critical Factors

The Report is based on the following important underlying factors:

- The municipal level of government in the Province is an order of government and properly deals with the Government of Prince Edward Island through a government to government relationship. This relationship between the Provincial Government and the

three municipalities in the Capital Region is extremely important and interdependent, and intrinsically supports and defines educational, social, and economic life in the Province. It is therefore critically important to the Province's own strategic objectives; most notably the Province's "Island Prosperity Strategy".

- Across Canada municipalities are experiencing a dual problem, perhaps best described by the Federation of Canadian Municipalities (FCM) as *"a growing gap between the services Canada's municipalities must deliver and what they can afford. These services are essential, yet the resources do not match the need. Compared with other orders of government, Canadian municipal governments have far fewer tools with which to raise revenue"*. Charlottetown, Stratford and Cornwall are in the situation described by the FCM.

- The situation is exacerbated by the "infrastructure deficit" which is defined as the difference between the legitimate demand for infrastructure and the capacity of municipal governments with their Federal and Provincial partners to meet that demand. The significant and growing infrastructure deficit in the Capital Region Municipalities is described in this Report. While new developments create revenues from the developer particular to the infrastructure improvements required by the development, existing infrastructure must be maintained by the tax base, user fees and conditional transfers on an ongoing basis.

- There are well-established public finance principles in Canada and around the world which are the proper basis to evaluate the Provincial decision to move from local property taxation to a municipal grant system. These include economic efficiency, fairness (equity), accountability, stability and predictability, autonomy, and ease of administration. The policy change to municipal grants is analysed in the Report in the light of these principles.

## 1.3 Findings

The findings in this Report were independently arrived at by the Consultants from information provided by the municipal clients and from other publicly available information. They are summarized as follows:

- The new municipal grant program, introduced by the Provincial Government in 2008 to replace the CUSA, is unacceptable to the Capital Region Municipalities.

- There will be a significant negative fiscal impact on the Capital Region Municipalities, based on the assumption provided by the Provincial Government that the municipal grants would increase annually in accordance with the increase in the Consumer Price Index. These potential impacts are detailed in the Report.

- Under the new municipal grant program, taxpayers in the Capital Region Municipalities will be paying the same rate of tax on residential properties as in the past under the CUSA, however, the Municipalities will be receiving significantly less revenue than they otherwise would had the tax credit system remained in place. The benefactor of the "lost" municipal revenue is the Provincial Government.

- For the taxpayers in the Capital Region Municipalities, reduction or elimination of services will mean they will pay the same amount of tax as in the past, but will receive less services in return. Alternatively, if the municipal tax rate is increased, taxpayers will receive the current level of service but will pay more for these services.

- The administration fee, formerly charged by the Province to all municipalities, was discontinued in 2008. By including the "saved" administration fee as an off-set in the calculation of the new municipal grants to each of the Capital Region Municipalities, the Province effectively "clawed back" the benefit whereas "non-CUSA" municipalities would not be similarly affected.

- Given the magnitude of the potential annual loss of revenue to the Capital Region Municipalities and the lack of available options by way of taxing power, the only choices available to them will be to reduce or eliminate services and/or to raise the municipal portion of the tax rate.

- Charlottetown, Stratford and Cornwall all face significant infrastructure deficits which cannot be properly addressed within the framework of current provincial/municipal fiscal arrangements.

- The change to a municipal grant system is not consistent with the generally accepted public finance principles upon which provincial/municipal relationships ought to be based.

- The policy change announced by the Province in 2008 was not a recommendation from the December, 2000 KPMG Report.

- It is clear that the trend in Canada has been to reduce provincial transfers to municipalities and to increase property taxes and user fees. The move away from "tax credits" as they were defined under the CUSA arrangements is, in fact, a move away from the trend in other jurisdictions. If the Province were to follow the Canadian trend, the policy direction would be to retain the tax credit system and increase the value of the credit.

- The Capital Region Municipalities must accept the responsibility of informing their citizens about the implications of the new grant system with respect to both service delivery and the tax rate in their communities.

- This is a complex situation which requires attention to clarity and a sense of urgency on the part of both the Capital Region Municipalities and the Provincial Government. There are better and more equitable ways to achieve the appropriate fiscal relationship between the Capital Region Municipalities and the Province of Prince Edward Island. These can best be explored through a collaborative process recommended in this Report.

### 1.4 Recommendation

**The significant financial and planning issues facing the Capital Region Municipalities, as a result of the introduction of the new municipal grant program in 2008, can only be resolved if there is a political will and determination to do so. To date, discussions among senior provincial and municipal public servants have failed to resolve the issues. Accordingly, we recommend an urgent meeting of senior political leadership, including the Premier, the Minister of Communities, Cultural Affairs and Labour, the Provincial Treasurer and the Mayors of the Capital Region Municipalities, with the objective of establishing a process with a clear mandate, tight timelines, funding support and designed to identify clear and equitable solutions. Time is of the essence in initiating this process.**

### 1.5 Conclusion

The issues that this Report attempts to address are not merely about money. While the numbers will show that it is reasonable to expect an ongoing and significant negative financial impact from the new municipal grant system on the Capital Region Municipalities, simply addressing that impact through some changes to the newly instituted municipal grant program, if that were possible, would fail to address the problem. **The key issue is about how the Capital Region Municipalities, who have commissioned this Report, can work together with the Provincial Government to best serve their mutual constituents; the citizens and taxpayers of these Municipalities.**

# 2.0 INTRODUCTION

## 2.1 Background

The Legislative Assembly of the Province of Prince Edward Island proclaimed the Charlottetown Area Municipalities Act (the "Act") on July 28, 1994. Part 1 of the Act provided for the creation of the City of Charlottetown as it is now defined and Part 2 for the creation of the Towns of Cornwall and Stratford. The creation of these communities was the result of an amalgamation of a number of smaller communities to create the City and the two Towns (collectively, the "Capital Region Municipalities"). Prior to amalgamation in 1995 there were a number of differences in the manner in which streets and policing services were provided within the Capital Region Municipalities. With amalgamation those arrangements were replaced by a Comprehensive Urban Services Agreement (CUSA).

The CUSA (the "Agreement") for Charlottetown provided that the Province would vest in the City of Charlottetown *"ownership of and responsibility for the maintenance of streets and highways in the City"*. In the case of Cornwall and Stratford the responsibility for maintenance of streets and highways was retained by the Province. In addition, the Agreement provided that *"effective April 1, 1995 responsibility for policing services within the City shall be assumed by the City"*. The former City of Charlottetown (pre-amalgamation) had provided police services since its original incorporation. In the case of Cornwall and Stratford the discussions surrounding the transfer of police services provided the municipalities with a choice. Cornwall opted to leave police services with the Province through the provisions of the Provincial contract with the RCMP. Stratford chose to accept the responsibility for police services in their community and entered into a contract directly with the RCMP for that purpose.

In the view of the Capital Region Municipalities the CUSA was to be the document where the principles governing the relationship between the two orders of government would be defined

and accepted. In their opinion, the Agreement fell short of that objective and merely set forth the basis for a funding mechanism that the Municipalities could rely on in association with the costs of policing and public works services. This funding mechanism is referred to as the "tax credit system". Through the tax credit system, the provincial tax rate on non-commercial realty in all three amalgamated communities was established at $1.00 per $100 of assessment. The Province turned over tax points equivalent to $0.20 per $100 of non-commercial realty assessment to reflect the CUSA negotiations. This applied to all three municipalities, Charlottetown, Cornwall, and Stratford. Charlottetown, the only municipality which retained responsibility for streets, received an additional tax credit in the amount of $0.46 per $100 of assessment. The municipal grant programs for policing and streets (the items referenced in the CUSA), as they applied to these Municipalities, were discontinued and, at the same time, other programs of support to some or all of these Municipalities were also discontinued. These discontinued programs included supports in the areas of recreation and planning. The principle on which the negotiations were based, from a Provincial perspective, was that the outcome would be revenue neutral to the Province.

In the Budget approved in the Legislative Assembly in 2008, government announced its intention to abandon the tax credit system outlined in the CUSA and replace it with a new municipal grant program. The intention was given effect in the same session of the Legislative Assembly with the enactment of Bill No. 26; *"An Act to Amend the Real Property Tax Act"*. At a meeting on May 22, 2008 in Cornwall, the Capital Region Municipalities were briefed by provincial staff on the new grant program that would replace the former tax credit system.

The City of Charlottetown and the Towns of Cornwall and Stratford have serious concerns about the impacts of that change from both a public policy perspective and a financial point of view. To date discussions with the Province have not found any willingness to address these concerns.

The Capital Region Municipalities engaged the services of a professional consulting firm; MacPherson Roche Smith & Associates (MRS&A) to provide a complete understanding of the

new municipal grant program and its implications for the Capital Region Municipalities. This Report provides an independent assessment of the situation which could form the basis for meaningful discussion with the Province with respect to the new municipal grant program.

The terms of reference for MRS&A's assignment are summarized as follows:

- Review the former CUSA funding arrangement, municipal services, and budgeting in the three Capital Region Municipalities to obtain a thorough understanding of the former funding system.
- Assess the impact of the Province's CUSA/tax credit decision on these Municipalities over the long term in terms of the impact on their ability (individually) to finance services and the potential impact on municipal tax rates.
- Evaluate the CUSA/tax credit decision against a number of established public finance principles (e.g. efficiency, equity, transparency, accountability, local autonomy, etc.).
- Provide tables/charts on the trend in municipal taxation and transfers to municipal governments by Province across Canada over the last 20 years, and compare and comment on the CUSA/tax credit decision in light of these trends.
- Provide and present a final report to the Capital Region Municipalities and the Provincial Government.

To assist in the study MRS&A engaged the services of Dr. Enid Slack. Dr. Slack is the director of The Institute on Municipal Finance and Governance at the Munk Centre for International Studies at the University of Toronto. She is one of Canada's foremost experts in municipal finance and an Adjunct Professor at the University of Toronto, teaching a graduate course in urban public finance to planning students. She has been working in this field for over 30 years and is respected nationally and internationally for her research on property taxes and other aspects of municipal finance. The co-author of four books, she has also published numerous articles on urban public finance. Her most recent book is entitled *"International Handbook on Land and Property Taxation"* (co-edited with Richard Bird).

## 2.2 Provincial/Municipal Relationship

This Report is developed on two basic premises:

- The municipal level of government in the Province was created and given jurisdiction by the Legislative Assembly of the Province of Prince Edward Island. It is therefore an order of government and deals with the Government of Prince Edward Island on that basis. The municipalities created pursuant to the Charlottetown Area Municipalities Act properly have a government to government relationship with the Government of P.E.I.

- There exists an extremely important and interdependent relationship among the three Municipalities in the Capital Region and the remainder of the Province; a relationship that intrinsically defines educational, social, and economic life in the Province.

It is important to examine and explain these basic premises at the beginning of this Report.

Municipal governments have long been recognized as serving at the heart of democracy. As the order of government closest to the people, municipal government has expanded in response to changing local needs. Municipal councils provide essential public services and infrastructure that meet citizens' needs. While the services provided may differ from municipality to municipality, these services can include streets, policing, fire protection, recreation, sewer and water, planning, street lighting, and other services. Municipalities also support development in their communities in a variety of ways through support to organizations such as cultural organizations, community groups, Chambers of Commerce, Downtown Charlottetown Inc., Tourism Charlottetown and the PEI Convention Partnership Inc., and many others.

In providing these services over the last twenty years municipal governments in Canada, and their provincial and national organizations, have become directly involved not only with their respective Provincial Governments but also with the Federal Government. This cross-government involvement recognizes that services provided at the municipal level play a critical role in economic and social development at all levels of jurisdiction.

Using the Provincial Government's recently announced "Island Prosperity Strategy" as an example of provincial/municipal interdependence, the development it intends to create will rely to a considerable extent on the environments and services of the Capital Region Municipalities to support the economic, social and cultural expectations of immigrants and new citizens drawn by successful development. If the Capital Region Municipalities are to provide the necessary environments and services, they must be challenged and permitted to operate in compliance with what have become generally accepted principles for municipal governments in Canada. In summary these principles are articulated by the Federation of Canadian Municipalities as follows:

- Accountability and transparency;
- Fairness (helping those in greatest need while ensuring all governments contribute their fair share);
- Fiscal, economic, social, cultural and environmental sustainability;
- Adequate, predictable, and stable funding;
- Long-term planning;
- Respect for provincial and territorial jurisdictions and local priorities;
- Partnership among all three orders of government;
- Program flexibility; and
- Non-partisanship.

Later in this Report, the specific principles which come to bear on the issue of tax related revenues will be examined in greater detail. The complexities involved in addressing these principles within the Capital Region Municipalities require a close and effective partnership among the three municipal governments, and with the Government of Prince Edward Island.

# 3.0 POLICY STATEMENT – FEDERATION OF CANADIAN MUNICIPALITIES

In March of 2008 the Standing Committee on Municipal Finance and Intergovernmental Arrangements for the Federation of Canadian Municipalities (FCM) approved a new Policy Statement on the subject which provides the Committee's name.

In this statement FCM articulated what it believes is *"a growing gap between the services Canada's municipalities must deliver and what they can afford. These services are essential, yet the resources do not match the need. Compared with other orders of government, Canadian municipal governments have far fewer tools with which to raise revenue"*.

The Policy Statement goes on to describe the municipal financial crisis in terms of *"tight fiscal circumstances, limited borrowing capacity and limited access to adequate sources of revenue"* while contending that the municipalities have few, if any, options which will permit them to eliminate the growing infrastructure deficit in the country.

The problem has come about, in FCM's view, because municipal governments have lost the fiscal ability to serve their citizens, support municipal services, and foster an environment that attracts talented individuals and investment. They argue that municipal revenue sources must be predictable, stable, and adequate to their responsibilities.

Three root causes that explain the tight fiscal circumstances of Canadian municipalities are described as follows:

- Excessive reliance on property taxes;
- The transfer of responsibilities from other governments; and
- Reduced financial transfers from other governments.

These root causes apply to the financial situations that currently exist in Charlottetown, Stratford, and Cornwall, and need to be carefully addressed in a consultative framework by the Provincial and Municipal governments which are involved.

One term that is often used to describe a major challenge facing municipalities is the "infrastructure deficit" which can be defined as the difference between the legitimate demand for infrastructure and the capacity of municipal governments with their Federal and Provincial partners to meet that demand. The infrastructure deficit in the three Capital Region Municipalities is significant. It includes the need for expanded and improved water supply in the region, the replacement of aging infrastructure in the core area of Charlottetown, the restructuring of the waste treatment system in Stratford to accommodate significant new development that has occurred, and critical redevelopment of core streets to accommodate expanded traffic flow and the resulting access and parking demands. To illustrate the significance of the requirement for investment, in Stratford alone the estimated cost to provide basic water and sewer service is $20,000,000. While new developments create revenues from the developer particular to the capital cost of the infrastructure improvements required by the development, existing infrastructure must be maintained by the tax base, user fees and conditional transfers on an ongoing basis.

The definition of the "infrastructure deficit" refers to the "capacity of municipal governments with their Federal and Provincial partners to meet that demand". In considering the issue of the capacity of municipal governments to meet demand, it is important to consider the requirements for:

- Capital funding for planning, engineering and construction;
- Operational funding to operate and maintain these facilities; and
- Capital funding to update and replace existing outdated infrastructure.

The assumption is often made that municipalities are able, in collaboration with the Provincial and Federal Governments, to create infrastructure for ".33 cent dollars", after which the infrastructure can be maintained through user fees and additional tax revenues generated from

the development that the infrastructure supports. It has been shown that this is not a valid assumption, especially in municipalities that have limited access to the property tax base. This is because the property tax base provides the only access which municipalities have to tax revenues that support **all** of the services that are called upon to provide.

To address the serious implications of the new Provincial approach to the sharing of property tax revenues, the Capital Region Municipalities have acted jointly in this initiative because of their realization that the impact of the change has important (if different) implications for each of them, as well as for other municipalities in the Province. This issue is also a Provincial issue in that it poses critical questions about intergovernmental relationships. As such the issue is about more than merely money. While the financial analysis will show that it is reasonable to expect an ongoing, negative financial impact from the new municipal grant system on Capital Region Municipalities, simply addressing that impact through some changes to the newly instituted grant program, if that were possible, would fail to address the underlying issue. The real issue is about how the Capital Region Municipalities can work together with the Provincial Government to best serve their mutual constituents; the citizens and taxpayers of these municipalities.

# 4.0 THE COMPREHENSIVE URBAN SERVICES AGREEMENT

As noted in the introduction, at the time of the amalgamation, and as part of the process, the Province entered into negotiations with certain municipalities for a new Comprehensive Urban Services Agreement (CUSA). The result was to be a service/taxation exchange based on the principles of equity, uniformity and fiscal management. It was clear that the agreements were to be cost neutral to the Province. All of the provincial documents leading up to the amalgamation, including the White Paper on Municipal Reform, the Moase Commission report, and the Province's response to the Moase Commission entitled "New Cities, New Towns", anticipated an agreement that would, as its name suggests, be comprehensive in nature. The CUSA essentially dealt with streets and policing in the new municipalities; a reality which in the view of the affected Municipalities does not represent a comprehensive approach.

The CUSA negotiations were separate with each of the affected municipalities. Summerside and Cornwall signed the CUSA while Charlottetown and Stratford did not. Even though they were not signatories to the CUSA, Charlottetown and Stratford both accepted responsibility for policing, and Charlottetown accepted responsibility for streets as well.

Charlottetown's reluctance to embrace the new arrangements resulted from a rather dramatic growth in service demand which was not taken into consideration in calculating the tax credit transfer to Charlottetown. For example, in the area of police services, based on policing provided in the communities surrounding the former City of Charlottetown, the estimated cost of police services in the amalgamated City provided for a nine person addition to the City Police Department. To meet actual demand the City was required to add an additional 18 police officers and to increase the administrative support staff accordingly. These kinds of inequities resulted in prolonged discussions, negotiations and lobbying efforts through which an agreement was

eventually reached between the City and the Province and given effect in a Memorandum of Understanding (MOU) which provided an additional $1.0 million per year in revenue to Charlottetown. The MOU also committed the two parties to a study which would examine the most appropriate level of government to provide specific services and would also examine the financial arrangements between the Province and the municipalities. When the terms of reference for the study were being drafted, Charlottetown and Stratford agreed to participate. Cornwall was also invited but chose not to participate. Through a competitive bidding process responses to a Request for Proposals were received from four firms. The national firm of KPMG LLP was selected to complete the study.

# 5.0 THE KPMG REPORT

KPMG LLP, in responding to the terms of reference, organized their December, 2000 report into four main areas:

- Roles and Responsibilities
- Streets and Roads
- Police Services
- Provincial/Municipal Funding

In the area of **roles and responsibilities,** KPMG recommended that the responsibilities be aligned as follows:

| Role | Responsibility |
|---|---|
| Local road, street maintenance and storm drainage | Municipality |
| Provincial road, street maintenance and storm drainage | Province |
| Industrial park management, service delivery and financing | Joint where practical and beneficial – should not be mandated |
| Financing the delivery of assessment, tax billing and collection services | Both levels of government |
| Financing library service delivery including facilities | Province |

In the area of **streets and roads,** KPMG recommended that the classification of street and road maintenance expenditures be standardized to better enable cost comparisons between the provincial and municipal governments. They also recommended that Stratford and the Province evaluate the cost-benefit of shifting street and road maintenance from the Province to the municipality in order to bring the arrangement in line with the typical practices in other jurisdictions.

In the area of **police services,** KPMG found it difficult to effectively deal with the issue in the absence of province-wide policing standards and recommended that the municipalities, in conjunction with the Province, should develop and implement such standards.

In the area of **Provincial/Municipal Funding**, the area which is perhaps most critical to this report, KPMG recommended that the *"provincial government* ***undertake a study*** *(emphasis added) of the tax credit system with an objective to replace the tax credit method of transferring property tax revenues from the Province to the municipalities with a series of conditional grants structured to more closely match the cost of delivering the service or at least the cost of delivering a service that meets a minimum uniform standard"*. The KPMG recommendation was for a study which, to our knowledge, did not occur. KPMG further indicated that there should be no significant change to funding for specific services, except for the examination of the potential change from a tax credit system to a conditional grants program.

It is important to note that the KPMG Report was neither accepted nor endorsed by any of the Capital Region Municipalities.

In the 2008 Budget Address the Provincial Treasurer, referring to government's objective of taking a close look at our Island's municipal framework, announced the intention to appoint a Commissioner on Land and Local Governance to conduct a thorough review, including a broad examination of the fairness, equity, and transparency of the provincial/municipal financial framework. At the same time, he noted that Government understood that improvements must be made to the relationship between the Province and its municipalities while this work was being done. In that regard he announced that:

- Government would no longer charge an administration fee to assess properties and collect property taxes;
- Government would begin to disburse payments to municipalities on a monthly basis; and
- Government would support a fully-funded equalization program, one that will ensure fairness and transparency.

The Municipalities in the Capital Region appreciate the value to municipalities across the Province of these changes, and understand that the changes were recommended by the Federation of Prince Edward Island Municipalities [FPEIM]. At the same time, the premise that underlines the approach taken by KPMG relates to the desirability of reasonably uniform standards in the provision of services. As these standards are established, the Provincial and municipal governments will need to take into account the shared responsibilities that are inherent in implementing them. This would clearly be a central consideration in the work of the Commissioner. It is inconsistent that Government would anticipate the Commissioner's work by sending the signal inherent in the change to a grant system, given that this change was neither the subject of any intergovernmental discussion or recommended by KPMG, nor was it recommended by the FPEIM. While not specifically mentioned in the 2008 Provincial Budget, as noted earlier, the government subsequently introduced the legislation which removed the tax credit system.

# 6.0 THE CHANGE FROM TAX CREDITS TO GRANTS

Subsequent to the enactment of the legislation the affected municipalities were briefed on a new municipal grants system that would be based on the principles outlined in a document provided by the Province to the municipalities on May 22, 2008. The document refers to the new grants program as the "New World" arrangement.

- 2008 "New World" base funding amounts are calculated using the following criteria:
  - Frozen equalization formula (2007 values).
  - Police tax credit based on 2008 assessment values (converted to a grant).
  - Street tax credit based on 2008 assessment values (converted to a grant).
  - Police grant based on $44.10/capita based on the 2006 census, for those municipalities previously receiving a police grant.
  - Streets grant based on $6,250/km, for those municipalities previously receiving a streets/highways grant.
  - The administration fee (based on 2008 assessment values) and the calculated Provincial interest expense incurred in converting from the existing method of three tax payment installments annually to monthly tax revenue payments have been calculated in as "credits", on the premise that these are costs that the municipalities no longer bear.

- 2008 "New World" transition funding is based on the following criteria:
  - Equalization was recalculated based on full funding with discontinued tax credits removed from the formula.
  - The Charlottetown and Summerside CUSA supplementary amounts were discontinued.

- 2008 “New World” transition funding will be implemented as follows:
  - Decreases in funding will be phased in over 3 years with funding top up provided at 66% in 09/10, at 33% in 10/11, and actual value in 11/12.
  - Year One will involve no net loss in equalization.
  - Year One becomes the base year for the municipal grants.
  - Year Two is projected to be based on the grants (former credits and former grants combined) being capped, and equalization based on the formula being calculated annually.
  - The new funding arrangement is intended to be an interim solution that may be affected by any forthcoming recommendation from the Commissioner on Land and Local Governance.

In the information provided with respect to the new grants system, note is made of the fact that several of the initiatives adopted were recommended by the Federation of Prince Edward Island Municipalities (“FPEIM”). Central to the position taken in the FPEIM February, 2008 Annual Submission to the Government of Prince Edward Island is the view that the Province should respect the relationship between municipal services and the ability to tax property. In its submission the FPEIM recommend *“that the Government of Prince Edward Island substantially reduce the provincial property tax rate within all municipalities and eliminate provincial property taxes within full service municipalities”*. In explaining their rationale for the recommendation it states in part: *“FPEIM continues to encourage the provincial government to provide property tax relief by substantially reducing the provincial property taxes levied within municipalities”*. Later in the same document they indicate that *“FPEIM is not suggesting that the provincial government is in a financial position to make enormous cuts to its property tax revenue in the current year, or that it should not collect property taxes to pay for municipal services it provides. The government is requested to take a serious look at what it can do to reduce the property taxes it collects within municipalities and to develop a plan to implement the above recommendation over a reasonable period of time”*. The move to a grant system and away from a tax credit system is in direct contradiction to the view of the provincial organization representing Island municipalities.

The expected financial implications of the new grant system for the Capital Region Municipalities are examined and analysed in Section 9.0.

# 7.0 THE PUBLIC POLICY PERSPECTIVE

The public policy perspective with respect to municipal government finance is addressed from three points of view as follows:

- A model of local government finance (the "benefit model").
- The public finance principles for evaluating various municipal financial tools and their implication for Charlottetown, Stratford and Cornwall in the new municipal grant arrangement.
- The trends in property tax and transfer funding of municipal services across Canada over the last 20 years.

## 7.1 The Benefit Model of Local Government Finance

In terms of economic theory, the major role assigned to local governments is to provide goods and services within a particular geographic area to residents who are willing to pay for them.[1] Given this role of local government, the "benefits received" principle is the appropriate starting point (Bird, 1994). According to the benefit model of local government finance, local government services, wherever possible, should be paid for on the basis of the benefits received from those services (Tassonyi, 1997; Duff, 2003).

[1] According to the public finance literature, local government should not do stabilization policy because they do not have access to monetary policy and because capital and labour flow freely across local jurisdictions. They should also not engage in redistribution because local efforts to address income disparities will likely result in the movement of high-income groups to low-tax areas and low-income groups to high-tax areas (Kneebone and MacKenzie 2003). Although local governments do engage in some redistribution through the act of taxing and spending, redistribution should not be the primary focus of what they do. See Bird & Slack (1993) for a discussion of the role of local government.

This model suggests that user fees and local taxes are appropriate to pay for most local services. User fees are appropriate to fund at least some portion of the costs of services such as water, sewers, garbage collection and disposal, transit, and recreation.[2]

In general, user fees are appropriate where there is a clear relationship between the fees charged and the benefits received, the taxpayer has the choice about the extent to which he or she uses the service, it is possible to collect the charge at a reasonable cost, and equity concerns can be addressed (for example, by lowering or waiving fees for low-income users).

User fees can play an important role in municipal finance by ensuring that governments do what people want and are willing to pay for.[3] These fees to users lead to efficiency in two ways (Bird and Tsiopoulos, 1997):

- They provide information to the public sector about how much users are willing to pay for the particular service.
- They ensure that citizens value what the public sector supplies, at least at its marginal cost (the cost to an additional user).

Under-pricing a service (or not charging for it at all) can result in over-consumption of that service. When users of the service are not required to pay for it and are unaware of the cost of providing it, they will demand more of the service than if they had to pay for it. The result may be interpreted by government as a signal that they should provide even more of the under-priced service. For example, user fees for water that are based on the marginal cost encourage water conservation, discourage water consumption in low-value uses, and postpone the time when new investment is needed (Dewees, 2002). User fees for garbage collection give consumers a financial incentive to reduce waste collection by reducing, re-using or recycling garbage.

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[2] There are externalities associated with services such as transit and recreation, however, which may require other sources of funding as well.

[3] See Bird, Richard and Thomas Tsiopoulos (1997) for an extensive discussion of the potentials and problems of user charges.

User fees are not appropriate to pay for all municipal services, however. Services with "public good" characteristics (for example, police and fire protection, neighbourhood parks, local streets, and street lighting) have collective benefits that are enjoyed by local residents but which cannot easily be assigned to individual beneficiaries. These services are more difficult to charge for and require some form of local benefit-based taxation such as the property tax.

The property tax allows individuals to express their demand for services where benefits are consumed collectively. In this respect, the property tax can be considered to be a generalized, or non-specific, user charge (Kneebone and McKenzie, 2003).

The property tax is considered to be appropriate for financing local services for at least two reasons:

- Real property is immovable - it is unable to shift location in response to the tax.
- There is a connection between the types of services funded at the local level and the benefit to property values (Slack, 2005 and Mintz and Roberts, 2006).

The property tax is similar to a benefit tax in that it approximates the benefits received from local services. Residential property taxes, in particular, are appropriate to fund local governments because they are borne by local residents.[4] Those who enjoy the benefits from services are required to pay for them.

Within the benefit model, there is also an important role for intergovernmental transfers. On efficiency grounds, grants are appropriate where services spill over municipal boundaries (for example, regional highways). If the municipality responsible for the service bases its expenditure decisions only on the benefits captured within its jurisdiction, it will likely under-allocate

[4] The non-residential property tax may be less appropriate for financing local government expenditures because they are partially exported to residents of other jurisdictions who are consumers of the products or services produced in those properties. Tax exporting reduces accountability because those bearing the burden of the tax are not the same as those enjoying the benefits. There is thus an incentive on the part of local residents to demand greater expenditures because some of the cost is borne by others.

resources to this service. One way to provide an incentive to allocate more resources to the service generating the externality is a transfer from the provincial government. The type of transfer that is appropriate for addressing externalities is a conditional, matching grant. The grant should be conditional in that it must be spent on the service which generates the externality. It should be matching to reflect the extent of the externality. For example, if 50 percent of the benefits of highway expenditures spill over existing municipal boundaries, the matching rate should be 50 percent.

On the basis of equity considerations, some municipalities are unable to provide an adequate level of service at reasonable tax rates compared to other municipalities. This inability to provide an adequate level of service in the absence of a transfer may occur for at least three reasons.

- Tax bases differ from one municipality to another and thus, to collect the same amount of revenue, a municipality with a small tax base must levy a higher tax rate than a municipality with a large tax base.
- The costs of providing public services may be higher in one municipality than another so that more tax revenues are required to provide the same level of service.
- The need for particular public services may be greater in one municipality than another thereby necessitating higher expenditures (and higher tax revenues).

Under these circumstances, an equalization grant is appropriate. These grants, sometimes small and sometimes large, are usually unconditional but can be used for specific expenditure categories (e.g. highways).

## 7.2 Public Finance Principles in the "New World" Grant System

Certain well-established public finance principles are useful in the design of municipal finance tools and can be used to evaluate the Provincial decision to move from local property taxation to a provincial grant (i.e. the "New World"). According to the benefit model of local government finance, services such as policing and local streets should be financed by local taxation and, in particular, the property tax. Provincial grants are only appropriate where services spill over

municipal boundaries and where there is a need for equalization. Moreover, the property tax is considered an appropriate tax for local governments because property cannot move out of the jurisdiction and because there is a direct connection between property values and the benefits from the types of services that municipalities provide. A local property tax also gives municipalities autonomy to make their own decisions about how to pay for the services that they deliver and makes them accountable for those decisions.

In terms of the generally accepted principles of public finance, each of which are described below, the following can be said about the move of the Province away from credits based on real property tax to a system of municipal grants.

1) ***Economic efficiency*** is concerned with the allocation of resources to the production of goods and services where society gets the largest possible bundle of goods and services. Economic efficiency is achieved when the user fee or tax per unit of output of the service received equals the extra cost of the last unit consumed (the marginal cost). The tax or fee indicates what consumers are willing to pay for the service and the marginal cost measures the cost of resources used up in producing that service (Bird, 2001; Bird and Tsiopoulos, 1997, 35-37). In terms of efficiency, marginal cost pricing (user fees) is not appropriate to pay for policing and local streets however, local property taxes are appropriate to relate the cost and benefits of these services. The "New World" approach established by the Province, while not a marginal cost system, in effect moves the funding of streets and policing away from property taxes (or credits related to them) to grants which have no clear relationship to the delivery cost of the service. This is inconsistent with the principle of economic efficiency.

2) **F*airness (equity)*** based on benefits-received is achieved when those who consume public services pay for them. When a good or service is purchased in the private sector, the purchaser (user) pays for it and derives the benefit (the reason for which the purchase was made). The same principle should apply in the provision of public sector services. Fairness based on ability to pay suggests that those with greater ability should pay more taxes. The ability-to-pay principle is less relevant for municipal governments because their primary

responsibility is to deliver services and not to redistribute income, as noted earlier. Concerns about the tax burden on low-income individuals should be addressed through income transfers from the Provincial or Federal governments and social assistance programs targeted to individuals in need.

It is clear that the new municipal grant system instituted by the Province fails to meet the test of fairness, if not immediately, then certainly in future years. The needs for streets and policing, as well as the costs, will change over time and the change will likely differ in various municipalities. These changes will result from aging of the infrastructure, demographic changes, inflationary pressures, increased public expectation and demand particularly related to environmental pressures. Without the ability to refer to property taxes, municipalities, unlike the provincial governments, have no options in raising the required monies. By allowing the grant to increase simply by the amount of inflation in subsequent years, the grant is not taking account of changes in any of these factors with the possible exception of inflationary pressures. For example, if policing needs grow more quickly in one municipality than another because of different demographics or different development patterns, the proposed municipal grant system will not accommodate these differences over time. A grant that increases with the rate of inflation will not result in a fair distribution of the grants among municipalities in future years.

3) **A*ccountability*** means that taxes (charges) and expenditures should be designed in ways that are clear to taxpayers so that policymakers can be made accountable to the taxpayers for the services they deliver and the costs they incur. The more direct the relationship between the beneficiaries of a government service and payment for that service, the greater is the degree of accountability.

Grant systems have less accountability than local taxation systems because the party making the spending decisions is not the same party as the one raising the funds to pay for them. Accountability is greater when local governments set out their own expenditure priorities for local services and are responsible for raising the revenues to pay for them.

In New Brunswick, the Commissioner on Local Governance, Mr. Jean-Guy Finn is examining this and other questions in that jurisdiction. The NB Commissioner's Report is not yet available; however he has sent clear signals in the local media about the direction that it will take. In an interview carried in the Telegraph Journal (Saint John's daily newspaper) the Commissioner is reported as indicating that *"the current system of the provincial government collecting some property tax revenue and sending large grants back to councils is eroding accountability to taxpayers"*. Under his indicated model, the Province of New Brunswick would still operate an equalization formula that would guarantee municipalities would be able to offer comparable levels of services at similar tax rates, but those unconditional grants would be dramatically reduced and instead the Province would get out of taxing commercial and non-residential properties.

The NB Commissioner is quoted in the same article as saying that *"the way to do that is to transfer the occupation of the property tax room to the municipalities and then to reduce the grant that goes to the municipalities. If you open up too many tax fields to be occupied by too many governments it is continuing the confusion"*.

4) ***Stability and predictability:*** Revenues should be stable and predictable so that municipalities can budget and plan for future expenditures. Property taxes, by their very nature, are reasonably stable and predictable. On the other hand, government grants have historically been affected by the financial situation of the granting government. The factors which create tight financial situations for provincial governments most often provide similar difficulties for municipal governments. The difference, as noted above, is that municipal governments have fewer options, especially when they do not fully occupy the property tax field. Grants which increase with inflation will only be stable and predictable if the granting province does not change the funding formula over time. The history of grants in Canada suggests that they are not always a stable and predictable source of funding for municipalities (see Slack, 2005). Historically, grants often vary in keeping with the fiscal situation of the donor government.

5) **Au*tonomy:*** It is widely recognized that municipal governments should have autonomy and flexibility to set their own priorities. This fits with their status as an order of government. Clearly, there is less local autonomy with the grant system than with the tax credit system in that the Province influences local spending decisions through grants. Providing municipalities with a greater degree of autonomy is also in the best interests of the Provincial Government because it provides for a clear delineation of responsibility and therefore enhances the ability of citizens to hold municipal government directly accountable for the provision of local services.

6) **E*ase of administration*** means that the time and resources to administer the financing tool should be minimized. Ease of administration is not particularly relevant to this report in that the property tax and grant systems are already in place. The change is unlikely to materially affect administrative costs. It should be noted, however, that any proposal to install a municipally administered property tax system, as opposed to the provincially administered system with credits accruing to the municipality, would need to be carefully considered in light of this principle.

# 8.0 TRENDS IN MUNICIPAL REVENUE SOURCES IN CANADA

Figure 1 contained in Appendix "A" summarizes the sources of municipal revenue (capital and operating combined) for all municipalities in Canada over the 20 year period 1988 - 2007. This is important information in that it establishes a part of the context for the current discussion. It should be noted, however, that it is difficult to meaningfully compare the Island situation with other jurisdictions in Canada because there are so many variables in terms of how various sources of revenue and expenditure are classified and reported in different Provinces.

At the same time it is clear that the trend in Canada has been to reduce provincial transfers to municipalities and increase property taxes and user fees. The Province's move away from "tax credits" as they were defined under the CUSA arrangements is, in fact, a move away from the trend in other jurisdictions. In Canada, property taxes increased from 44.6 percent of total municipal revenues in 1988 to 46.8 percent in 2007; user fees increased from 20 percent to 22.2 percent over the same period. Provincial transfers, on the other hand, fell from 22.2 percent of municipal revenues at the beginning of the period to 17.2 percent at the end of the period. Federal transfers have always been a relatively small percentage of municipal revenues; however they have increased somewhat since 1988. Other revenues (such as investment income, fines and penalties, etc.) have remained roughly the same.

Contrary to the reference in the KPMG Report which suggests a trend in Canada to municipal grants, the opposite appears to be true. Municipal services in Canada are increasingly being paid for by property tax revenues and, where appropriate, user fees. If the Province of PEI were to follow the Canadian trend, the policy direction would suggest retaining the tax credit system and increasing the value of the credit.

In its annual submission to the Government of Prince Edward Island the FPEIM used some important references to describe the situation articulated in this Report. Its references are provided verbatim from their submission.

FPEIM begin by quoting from the Standing Senate Committee on National Finance as follows: *"It was clear to the committee that municipalities are struggling to meet their individual expenditure needs with current revenue sources. Municipalities do not have the same taxation powers as other orders of government and continue to depend largely on a narrow set of revenue tools: namely property taxes, user fees, and intergovernmental transfers."*[5]

The FPEIM submission also quoted from the External Advisory Committee on Cities and Communities. *"Property taxes are not an adequate base for municipalities to meet their infrastructure challenges. As it reduces the burdens of its own taxes, the federal government should encourage provinces and territories to provide cities and communities with a more substantial degree of autonomy in raising revenue."*[6]

The Conference Board of Canada is also quoted as stating that *"The most glaring shortcoming of the current taxation structure in Canada is the lack of flexibility in taxation instruments at the municipal level."*[7]

As well, the Canadian Tax Foundation is quoted to underscore the consensus that municipalities need to be supported in the current reality. *"The time has come for provincial governments to give municipalities access to additional tax sources."*[8]

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[5] Standing Senate Committee on National Finance, Second Interim Report on the Committee's Study on the Fiscal Balance between the Different Levels of Government in Canada, June 2007.

[6] External Advisory Committee on Cities and Communities, From Restless Communities to Resilient Places: Building a Stronger Future for All Canadians, June 2006, page ix.

[7] Anne Golden, Glen Hodgson, and Mario Lefebvre, Sustainable Funding for Canada's Cities, Conference Board of Canada, January 2008, page 1.

[8] Harry M. Kitchen, Canadian Tax Paper No. 107: Municipal Revenue and Expenditure Issues in Canada, Canadian Tax Foundation, 2002, page 336.

The Capital Region Municipalities currently have limited access to property taxes, limited room to increase or expand user fees and, as this Report suggests, an inability to play their proper role as municipal governments under the new grant system which cannot be seen as a stable and predictable funding source. A clear approach to revenue sharing that respects the generally accepted principles of public finance and municipal governance is urgently required.

Dr. Enid Slack, one of Canada's foremost experts in municipal finance is quoted as stating that: *"International experience teaches us that for municipal governments to be responsible, accountable and efficient, they need to raise their own revenues. Canadian experience shows us that local governments have been relying more heavily on property taxes and user fees and less on provincial governments in the last twenty years. The move to abandon the tax credit system in PEI and replace it with a municipal grant program moves in the opposite direction to what we have learned".*

# 9.0 FINANCIAL IMPLICATIONS – CHANGE FROM TAX CREDIT TO GRANT SYSTEM

## 9.1 The Provincial Municipal Fiscal Relationship Since Amalgamation

Until 2008 funding for the Capital Region Municipalities from the Province was provided through the Comprehensive Urban Services Agreement (CUSA). This Agreement has governed the provincial/municipal fiscal relationship since the amalgamation of a number of communities into the municipalities of Charlottetown, Stratford and Cornwall in 1995. As discussed previously, the Agreement provides property tax credits to the municipalities who are parties to the CUSA so that these municipalities are able to raise their respective property tax rates.

Charlottetown has also signed an additional funding agreement hereinafter referred to as "Supplementary CUSA". The Supplementary CUSA provided an additional $1,000,000 per annum to Charlottetown for the correction of a past miscalculation in the CUSA funding formula whereby certain streets within municipal limits, along with increased maintenance costs on core city streets, were not included.

In addition to funding under the CUSA, the Province also provided funding for certain municipalities under an equalization program which attempts to allow for the provision of similar services at similar levels of taxation within all of the municipalities across the Province. The formula used in the equalization funding arrangement for determining a municipality's equalization payment is as follows:

**A/100 X B X (C/D - E/B)**

Where:

A = the municipality's non-commercial property tax rate

B = the municipality's population

C = the provincial property tax assessment[1,2]

D = the total provincial population[1]

E = the municipality's property tax assessment[2]

[1] "provincial" only refers to incorporated municipalities

[2] "property tax assessment" includes both the commercial and non-commercial assessment

The Province announced in the 2008 Budget Address that it would both fully fund the equalization formula and properly apply the funding formula. Individually and through the FPEIM, the municipalities have argued for a number of years that the equalization program was not being fully funded and that the formula was not being correctly applied; thus they were not receiving the payments to which they were entitled. These specific changes were supported by the FPEIM. The Province made these changes at the same time as they announced the conversion from a tax credit system to a municipal grant system.

As important as it is to acknowledge the equalization changes given effect by the Province, it is also important to understand that the matter of sharing revenue from non-commercial realty taxes is a separate and distinct matter. Equalization exists to address inequities that exist between municipalities for a variety of reasons. Non-commercial realty tax exists to fund essential services in support of property and its development. The tax credits were intended to ensure that municipalities had the fiscal capacity to meet the legitimate essential services which are properly delivered by their order of government. Tax credits and equalization are different in nature and in application and must be seen to be separate and apart from each other. The change to a grant system from a tax credit system was not supported by the FPEIM and is, in fact, contrary to their expressed viewpoint.

## 9.2 The Immediate Impact of the "New World" Grant System

In addition to the fact that the announced grant system is contrary to established principles of public financing, as alluded to earlier in this Report, there are also immediate financial impacts to certain municipalities with respect to both the change from tax credits under the CUSA to municipal grants, and equalization.

The Province, in documents provided to the Capital Region Municipalities, has lumped together payments under the new grant system and equalization with implied cost savings from the elimination of administration fees and the increased frequency of property tax payments in order to demonstrate that the Capital Region Municipalities are better off under the new system than under the former CUSA system. In reality, however, the grants and equalization are separate funding sources that must be looked at individually. CUSA and the New World grant system are both funding mechanisms for services delivered by the Capital Region Municipalities that are provided by the Provincial government to municipalities in other areas of the Province. Equalization, on the other hand, is a mechanism for achieving the fairness principle, as discussed in Section 7.2. Equalization allows for municipalities with lower assessment bases to achieve levels of service reasonably similar to other municipalities with similar levels of taxation. Given this fact, one must first look at the core funding mechanism before assessing the impact of the equalization program.

**Core Funding**

***Charlottetown***

Charlottetown's original 2008 budget for transfers from the Province (including the value of the property tax credit, but excluding equalization) was $12,281,408, comprised as follows:

| | |
|---|---:|
| Property tax credit | $10,801,408 |
| Supplementary | 1,230,000 |
| Salt credit | 250,000 |
| Total | $12,281,408 |

Under the New World grant system, Charlottetown's revised 2008 budgeted amount is as follows:

| | |
|---|---|
| Provincial Grant | $10,801,408 |
| Transition Funding | 363,000 |
| Salt credit | 250,000 |
| QEH Grant-In-Lieu | 140,000 |
| Total | $11,554,408 |

The overall negative impact on the City is as follows:

| | |
|---|---|
| Provincial Transfers-Old system | $12,281,408 |
| Provincial Transfers-New system | (11,554,408) |
| Total Funding Decrease | $ (727,000) |

Information provided by the Province detailing the effect of changes from a tax credit system to a grant system shows a positive net impact for Charlottetown in the amount of $89,158. This is achieved in part by offsetting the above noted $727,000 shortfall with administration fee savings and implied interest savings due to increased property tax payment frequency. While it is true that the foregone administration fee will result in savings to Charlottetown in the amount of $432,000, by including these savings in the calculation of the New World grant the Province effectively "claws back" the administration fee savings that all non-CUSA municipalities throughout the Province will actually receive.

The Province has calculated the "savings" to the City in interest expense due to advancing funds monthly to be $287,158, however, this calculation is based on the projected cost of the measure to the Province, not on actual savings to the City. The City actually expects the effect of the increased frequency of tax payments to result in $65,000 in additional interest income to the City, but no reduction in interest expense. This $65,000 amount is, in fact, the real "savings" to the City.

The end result is that while the New World system will have an initial positive financial impact on all of the non-CUSA municipalities (and on certain CUSA municipalities) throughout the Province, the City of Charlottetown actually see an initial reduction in its core funding. It should also be noted that the changes to the property tax system were announced almost half way through the City's fiscal year. This has resulted in a situation where the City has committed to certain expenditures based on its original balanced budget, but must now deal with a significant reduction in its budgeted revenues. There are serious concerns the City eventually may have to reduce vital services, such as fire and police protection, in order to remain on budget.

The lack of communication between the Province and the City with regard to the unilateral change to the New World system has clearly placed the City in a difficult financial situation.

***Stratford***

Under the previous tax credit system, Stratford's budget for 2008 transfers from the Province consisted of a provincial tax credit with a value of $901,516. Under the New World system, this tax credit has been replaced by a grant with an equal value.

The Province's calculations show that Stratford will be better off under the New World System by $97,964, however, as with Charlottetown, this is due to the reduction in the $59,000 administration fee charged by the Province, and on interest "savings" due to increasing the frequency of payments to the municipalities. Again, the Province's interest savings calculations are based on the Province's cost to provide the more frequent payments. In reality, Stratford will realize minimal savings estimated at $14,000 from reduced interest expense, as it normally maintained a cash balance throughout much of the year prior to the switch to monthly payments. Therefore, the real savings are as detailed below:

| | |
|---|---|
| Provincial Transfers-New system | $ 901,516 |
| Provincial Transfers-Old system | (901,516) |
| Add: interest savings | 14,000 |
| Add: reduction in administration fee | 59,000 |
| Total Funding Increase | $ 73,000 |

While Stratford's funding for 2008 shows an improvement, it is clearly not adequate to offset the projected future funding shortfall described in Section 9.3. More importantly, the switch to a grant system has eroded both accountability to taxpayers and the autonomy of the Stratford Municipal Council.

***Cornwall***

Information provided by the Province detailing the effect for Cornwall of changes from a tax credit system to a grant system shows a positive net impact from the switch to the new world system in the amount of $233,310. The Province calculates this positive impact by including increased equalization payments, the reduction in the administration fee charged by the Province and interest "savings" due to increasing the frequency of payments to the municipalities. In reality, however, Cornwall will not realize any savings from reduced interest expense, as it presently maintains a cash balance throughout the year. As noted previously, equalization is a separate program and must be evaluated separately. Therefore, the only real savings come from the elimination of the administration fee, as detailed below:

| | |
|---|---|
| Provincial Transfers-New system | $ 432,789 |
| Provincial Transfers-Old system | (432,789) |
| Add: reduction in administration fee | 26,000 |
| Total Funding Increase | $ 26,000 |

While Cornwall is clearly a beneficiary in the short term of the announced changes in 2008 to the *equalization* program as discussed below, there appears a significant future negative impact, as projected in Section 9.3, on its core funding.

**Equalization**

The Province's 2008 decision to fully fund the equalization program and to properly apply the funding formula has been applauded by the municipalities, as it is more transparent and allows for more effective short and long-term planning. Indeed, the Federation of PEI Municipalities

had been lobbying for such a change in order to provide greater stability and predictability in funding for the municipalities.

For Charlottetown and Stratford, the change has meant that they are no longer eligible for equalization funding. The Province has offered transition funding, providing a three year phase-in of the decrease in payments these municipalities receive. The total amount of funding that each previously received comprised a very small percentage of their respective budgets; 0.2% of revenues in Charlottetown and 0.4% in Stratford. The impact on Cornwall, on the other hand, is positive in the short-term and relatively much larger.

Prior to the changes announced in the 2008 Budget Address, Cornwall expected to receive $58,240 as an equalization grant, amounting to 2.6% of its budgeted revenue. By fully funding the equalization program and applying the formula, Cornwall's equalization payment should have increased to approximately $327,751 (12.9% of budgeted revenues), as calculated in Appendix B using figures provided by the municipalities. However, the Province's decision to replace the provincial tax credit system under CUSA with a grant system resulted in a decrease in the municipal non-commercial tax rates in those municipalities previously funded through CUSA. This resulted in a reduction in Cornwall's equalization payment (see Appendix B) to approximately $228,432, or 9.3% of its budgeted revenues. The actual payment, based on guidance from the Province, will be $247,595.

The result is that while equalization is now "fully" funded by the Province, the extent to which it is funded has been diminished by the reduction in municipal rates brought on by the change from a tax credit system to a grant system. This decrease in municipal tax rates, achieved by moving to a grant system, is contrary to the principles of stability and predictability both in its implementation and its end result. The lack of consultation with the Municipalities made the shift unpredictable and the change in the municipal tax rates has resulted in instability in the funding arrangement.

While Cornwall welcomes the full funding of the equalization program, they also realize that equalization is not necessarily a permanent funding source. Equalization is not based on

increased or decreased needs within the municipality, but on the relative ability of the municipality to raise revenues compared to other Island municipalities. If other municipalities experience a decline in their tax base, or if Cornwall experiences growth in its tax base, the equalization component of Provincial funding will decline. Cornwall, and other municipalities, need stable, predictable funding so that they are not dependant on equalization.

### 9.3 The Projected Future Impact of the "New World" Grant System

The analysis above shows that there is a positive impact in 2008 from the changes announced in the 2008 Budget Address on both Stratford and Cornwall, and a significant negative impact on Charlottetown in the short term. More important, however, is the expected long-term impact of these changes.

In assessing the long-term impact, equalization has been excluded because it is a separate program with a separate goal from the core funding mechanisms of either the tax credit or grant systems. Also excluded from the analysis is the value of the administration fee elimination and the savings from more frequent property tax payments, as it is inequitable to offer all non-CUSA municipalities a "windfall" from these measures while, at the same time, effectively clawing it back from the former CUSA municipalities. Assumptions were also required to be made for the growth factor to be used in projecting the future value under both the former tax credit system and the New World grant system.

Tax Credit System

Under the former tax credit system, the driver for the value of the credit was the residential property tax assessment. In order to project the growth of the residential assessment, the average annual growth factors over the past five and ten year periods were examined. The recently announced freeze on assessments for a limited period (to 2010) will have a short term impact which will be resolved when the freeze is lifted. As understood by the municipalities, it was never the Province's intent that the assessment freeze would be long term in nature, especially

since it is contrary to the purpose of the Real Property Tax Act i.e. that assessment be a balanced representation of market value.

The average annual growth factors for the Capital Region Municipalities were as follows:

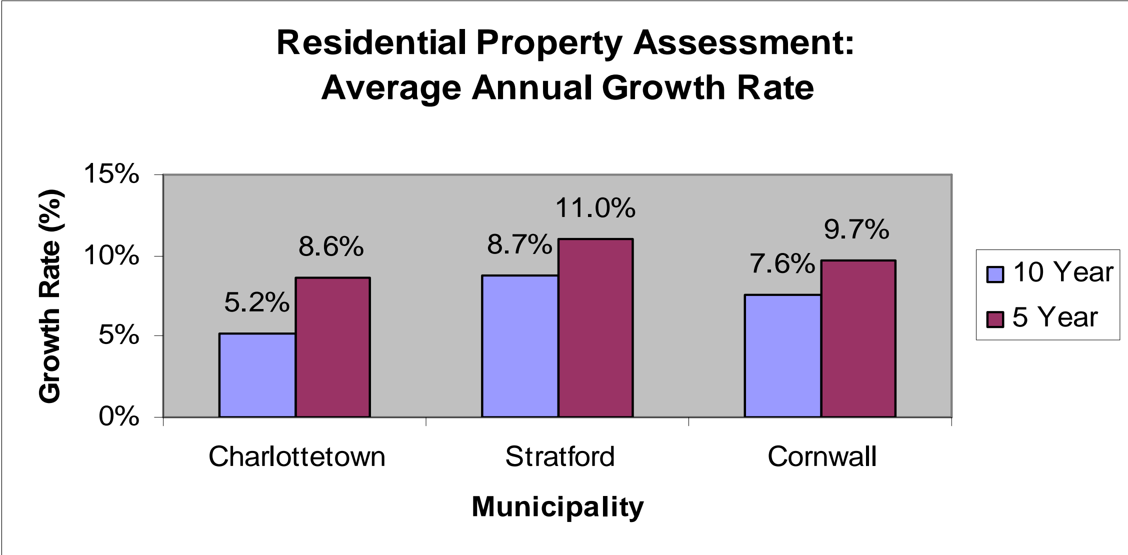



Figure 1: Residential Property Assessment: Average Annual Growth Rate

As can be seen from Figure 1 above, growth rates over the last five years were considerably higher than over the last ten years. This is consistent with the strong real estate market throughout the Municipalities and across Canada during this time frame. Given the exceptionally strong growth over the past five years, it is believed that the more conservative ten year average is more reflective of the sustainable average annual growth in residential property assessments in the municipalities in question. The ten year average growth rate is therefore used in projecting the implied future value of the property tax credit.

Grant System

Given the uncertainty surrounding the implementation and the future terms and conditions of the New World grant system, the only known factor upon which to project growth in the grant is the Consumer Price Index (CPI). Furthermore, this is the only factor set forth by the Provincial

Government on which the grant would be indexed. In order to remain consistent with the growth factor used in projecting the implied value of the tax credit system, the average annual growth in the CPI for the last ten years (1998 – 2007) was examined. For the last ten years the average annual growth in CPI has been 2.6%. A comparison of the growth factors used in the projections, as noted in Figure 2, highlights the large discrepancy expected between the growth in CPI and the growth in residential assessments.

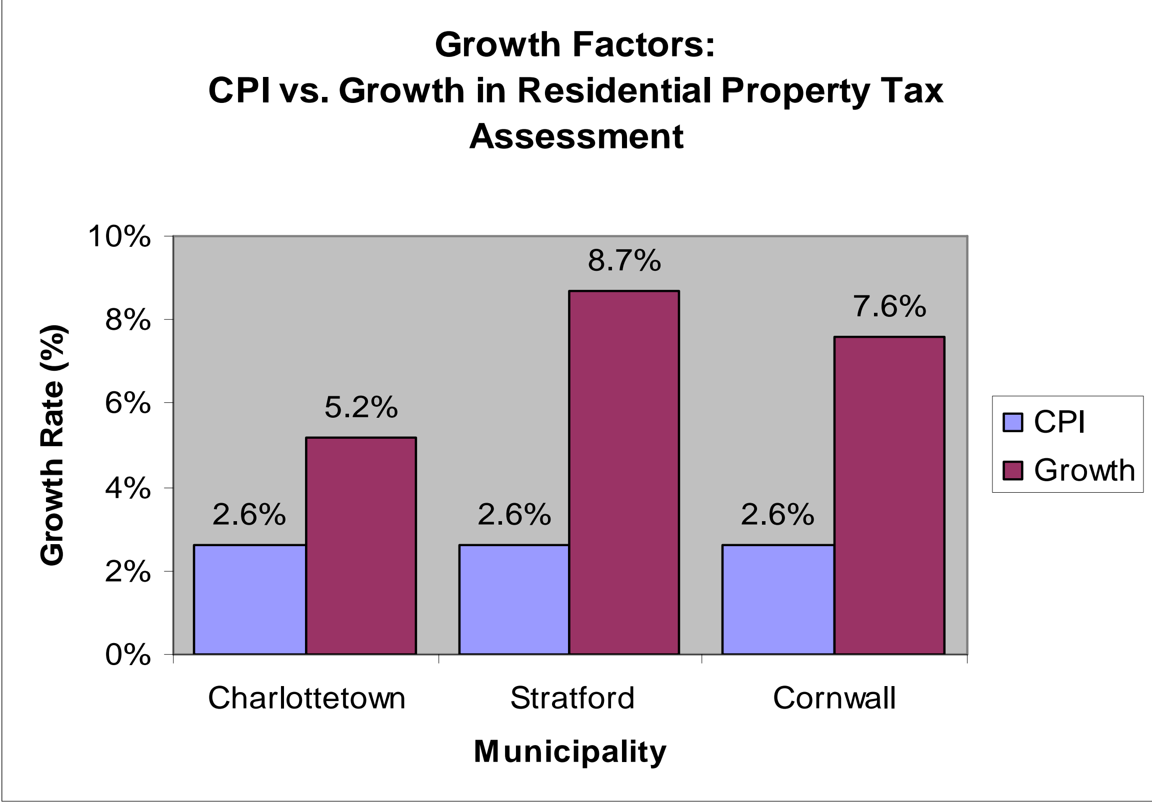



Figure 2: Growth Factors: CPI vs. Growth in Residential Property Tax Assessment

Using the above noted growth factors, the projected value of the New World grant system for the next ten years was compared to the projected value under the former tax credit system. As illustrated in Appendix C, the discrepancy between the new grant system and the former tax credit system quickly accelerates. After only ten years, the cumulative negative financial impact on the municipalities is projected as follows:

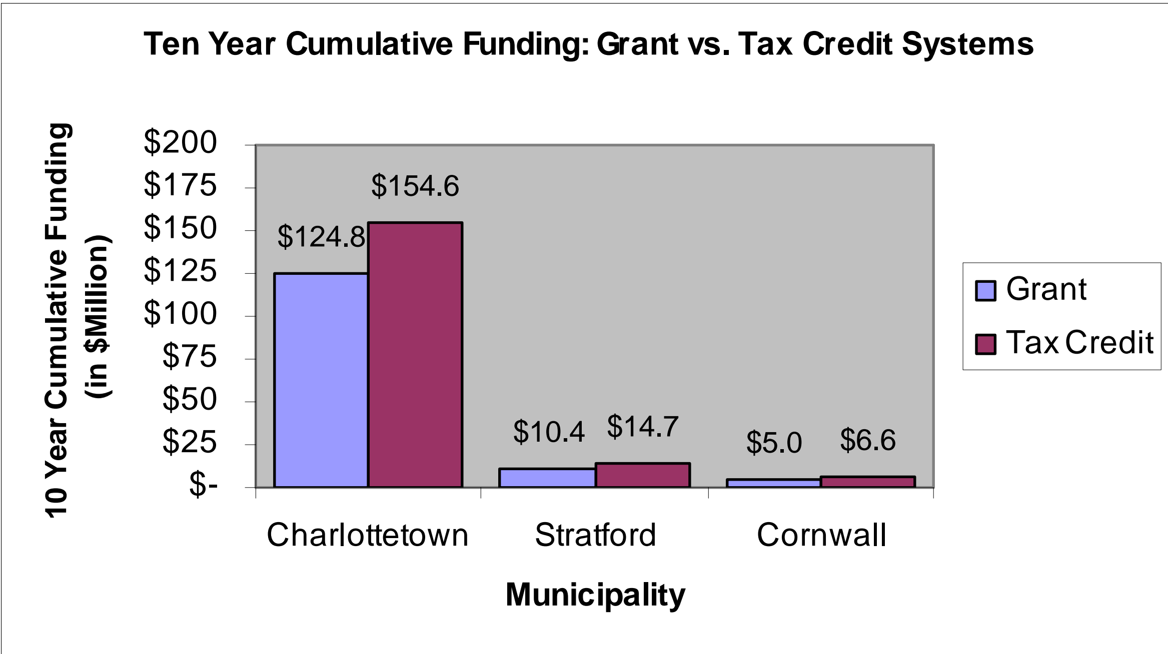



Figure 3: Ten Year Cumulative Funding: Grant vs. Tax Credit System

Figure 3 highlights the significant negative financial impact, over the 10 year period 2009 – 2018, on the Capital Region Municipalities from the implementation of the New World grant system. For Cornwall, the negative impact amounts to approximately $1,600,000 less in cumulative funding over 10 years. For Stratford, the negative impact is over $4,300,000, while in Charlottetown there is a significant projected negative impact of almost $30,000,000, which is in addition to the estimated $727,000 funding shortfall in 2008.

For illustrative purposes, we have projected the potential increase to the municipal tax rates of the Capital Region Municipalities based on the assumptions that the new municipal grant system came into effect in 1998 (rather than 2008) and that annual revenue shortfalls (as compared to actual revenue under the tax credit system) are recovered through increases to the municipal tax rate. As shown in Appendix D, each of the Municipalities would have experienced revenue decreases each year over the 1999 – 2008 period. By 2008, the assumed replacement of the tax credit system with the municipal grant system is projected to have resulted in increases to the 2008 municipal tax rates (per $100 of assessment) over the 1998 base year of $0.08 (12%) for Cornwall, $0.09 (14%) for Stratford and $0.17 (13%) for Charlottetown. On a residence

assessed at $200,000, this would translate to an approximate increase in 2008 municipal tax of $160 per year in Cornwall, $180 per year in Stratford and $340 per year in Charlottetown, in order to maintain services at their current 2008 levels in each of the Municipalities. As illustrated in Figure 3, the discrepancy between projected revenues under the tax credit system compared to the municipal grant system continues to grow annually over the ten year period 2009 – 2018, potentially resulting in further annual increases to the municipal tax rate in each of the Capital Region Municipalities.

Clearly, the potential negative impact of the change to the New World grant funding mechanism on the Capital Region Municipalities is significant and must be addressed. This becomes particularly evident when, as illustrated in Figure 4, the ten year average growth in CPI is compared to the historical growth in municipal expenses for the same period. If the New World grant system uses only CPI as the growth factor for continued funding, the potential negative impact on the future delivery of services becomes readily apparent.

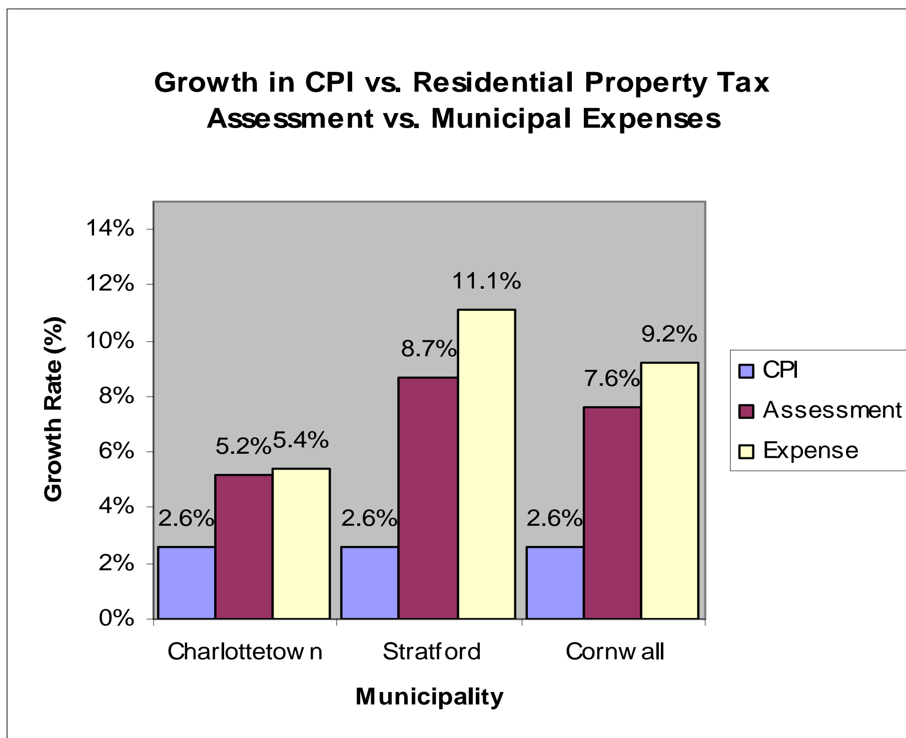



Figure 4: Growth in CPI vs. Residential Property Tax Assessment vs. Municipal Expenses

The former tax credit system, while not viewed by the Capital Region Municipalities as the optimal funding mechanism, had two important advantages over the New World grant system. First, under the former property tax credit system there is a much closer correlation between growth in the tax credit and growth in municipal expenses. This is due to the use of residential assessment growth as the revenue driver. Under the New World grant system, the use of CPI as the only growth factor in grant funding will result in the ongoing delivery of services at current levels requiring increases to municipal tax rates, which in turn will result in the affected municipality becoming uncompetitive compared to surrounding municipalities. As discussed in Section 7.2, this situation is contrary to the fairness principle because funding is no longer based on the needs of the demographic residing within the municipality, but on the increase dictated in accordance with growth in the CPI. As seen in Figure 4, there is no correlation between the rate of growth in the CPI and the rate of growth in expenditures in the Municipalities, thus an inequitable situation will be rapidly created among the municipalities. The need for services and the cost of these services change over time and will likely differ among municipalities. The changes in expenditure levels among municipalities result from variables such as aging infrastructure, inflationary pressures, demographic changes, demand related to environmental pressures and increased public expectations.

The second advantage which the property tax credit system had over the grant system is that it provided better accountability. Increasing the proportion of the municipality's budget that is composed of grants diminishes the relation between taxing decisions and spending decisions, which in turn reduces accountability and creates confusion for the taxpayer. This disconnect will continue to fuel the ongoing "blame game" and "finger-pointing" that arises between the provincial and municipal orders of government.

## 9.4 Who Benefits from the Change?

Apart from the projected declining revenues for the municipalities through a grants system as opposed to a tax credit system, nothing changes except by way of projected development and projected increases in the Consumer Price Index. The Provincial tax rate of $1.00 per $100 of assessment remains the same. The taxpayers will be paying the same Provincial tax rate as in the

past, however, the municipalities will be receiving less revenue. The benefactor of the "lost" municipal revenues is the Province. Given the lack of options available by way of taxing power to the municipalities, the only choices will be to cut services and/or raise the municipal portion of the tax rate.

For the taxpayers in the Capital Region Municipalities the potential outcome of the change from the tax credit system to the municipal grant system is quite evident. Reduction or elimination of services will mean they pay the same amount of tax as in the past, but will receive less services in return. Alternatively, if the municipal tax rate is increased, taxpayers will receive the current level of service but will pay more for these services. The Capital Region municipal councils should, in the interest of both transparency and accountability, explain clearly to their citizens/taxpayers the potential implications of the situation in which they have been placed as a result of the Province's unilateral decision to replace the former tax credit system with the new municipal grant system.

# 10.0 CONCLUSIONS AND RECOMMENDATION

## 10.1 Conclusions

The existing Provincial/Municipal fiscal relationship is viewed as an urgent and important matter by the Capital Region Municipalities of Stratford, Cornwall, and Charlottetown. In the short term these municipalities are within two months of beginning a new fiscal year. In the long term they are facing an uncertain future with a radically different approach to Provincial/Municipal fiscal relationships. This should also be seen as an urgent and important matter for the Province of Prince Edward Island. The success of the ambitious agenda outlined in the Province's "Island Prosperity Strategy" depends, to a significant degree, on a number of important structural factors including the economic, social, cultural and infrastructure health of the Capital Region Municipalities. These are the Municipalities which will provide the core services for the new generation of Islanders and talented newcomers to PEI, who are expected to find exciting and rewarding careers in the expanded economic sectors targeted by the Strategy.

In the new economy envisioned by the Island Prosperity Strategy it is important to anticipate changing demands related to environmental, cultural, educational, demographic and quality of life standards. These demands must, to a significant extent, be met by the Capital Region Municipalities within the framework of urban municipal governance.

For the Capital Region Municipalities to respond to the challenges posed by the Island Prosperity Strategy, they will need to change and grow in a way that is consistent with the new vision of prosperity. The ability to achieve this redefinition within the structure of Municipalities in the Capital Region requires a carefully defined and cooperative relationship with the Provincial Government, particularly in the areas of taxing power and fiscal management. The following considerations will be especially important to that relationship:

- An appreciation of the challenge of limited resources that faces both orders of government.
- A clear understanding of the interdependence that exists between the two orders of government.
- A collaborative approach to meeting those challenges that respects the generally accepted principles for defining and managing provincial/municipal fiscal relationships in Canada.
- A clear understanding and mutual acceptance of the principles that define the way in which municipalities will be empowered to define their revenue sources so that there is a fair distribution of access to the tax system as it relates to the level of accountability for services. These principles include economic efficiency, equity, accountability, stability, predictability, autonomy, and ease of administration.

Just as surely as it is not tenable for the Province to meet the challenge of growth in the exciting new economy that is envisioned without effective partnerships with the Capital Region Municipalities, neither is it possible for these Municipalities to create the kinds of communities that will be needed unless there is a principled and equitable fiscal arrangement existing between the Provincial and Municipal levels of government. If the two orders of government can work together to address these issues, new and more effective long-term approaches can be created that will better serve the interests of both orders of government, as well as those of the citizens/taxpayers to whom they are mutually accountable.

**The "New World" requires more than simply a debate about how the money is allocated. What is required is an open and enduring government to government relationship that can result in new ways to jointly build a prosperous future for the Province.**

Our examination of the existing Provincial/Municipal fiscal relationships concludes that:

- The New World grant system will seriously affect the fiscal situation of the Capital Region Municipalities in both the short term and the long term.

- There are better ways to respect the generally accepted principles that govern public finance and Provincial/Municipal fiscal relationships.
- The situation must be seen as **urgent** by both orders of government.

More importantly, we conclude that little or nothing will be accomplished by finger pointing, assigning blame, and positioning for aggressive negotiations. In the jargon of the labour movement this is the time for an "interest based" process. The two levels of government share important joint interests which they need to understand and explore together on a "clean page" basis, in an environment that is open to seriously considering meaningful and important change.

### 10.2 Recommendation

In considering the best way for the Capital Region Municipalities to approach the Provincial Government in connection with this urgent matter, and in anticipating the most appropriate response from the Provincial Government, a number of options were evaluated.

One option would be for the Capital Region Municipalities to ask that the Province add the issue to the terms of reference of the soon to be announced Commissioner on Land and Local Governance. This option was rejected because the new Commission will be required to address a much broader range of issues related to municipal governance across the whole of the Province. This will make it virtually impossible for the Commission to respond in the urgent way required by the situation currently facing the Capital Region Municipalities.

Another option would be for the Province and the Capital Region Municipalities to agree on the appointment of a new Commissioner who would be charged with the specific challenge of examining the important issues facing the Capital Region Municipalities and the Province with respect to financing local government in accordance with the generally accepted principles of public finance that are articulated in this Report. This option was also rejected because such a Commission would be a time consuming process and would not assure the urgently required development of more effective relationships between the two orders of government.

In the opinion of the Consultants, the most appropriate and expedient way to address the situation is for Capital Region Municipalities and the Provincial Government to enter into an agreement for the creation of a small team of senior municipal and provincial public servants who would consider, with the guidance of an independent chair, the issues raised in this Report and bring back to the Provincial Cabinet and Municipal Councils some clear recommendations to address them. This cooperative approach is the best, and perhaps the only way for the two orders of government to achieve the required redefinition of the Province's fiscal arrangements with the Capital Region Municipalities, particularly in the area of taxing power and fiscal management. The generally accepted principles of public finance noted and articulated in this Report demand nothing less.

## Recommendation

**The significant financial and planning issues facing the Capital Region Municipalities, as a result of the introduction of the new municipal grant program in 2008, can only be resolved if there is a political will and determination to do so. To date, discussions among senior provincial and municipal public servants have failed to resolve the issues. Accordingly, we recommend an urgent meeting of senior political leadership, including the Premier, the Minister of Communities, Cultural Affairs and Labour, the Provincial Treasurer and the Mayors of the Capital Region Municipalities, with the objective of establishing a process with a clear mandate, tight timelines, funding support and designed to identify clear and equitable solutions. Time is of the essence in initiating this process.**

## The Challenge

The Throne Speech delivered by the Lieutenant Governor of the Province to the opening of the Legislative Assembly in April of 2008 states the following:

***"As we confront future challenges, my Government is calling upon Islanders to embrace a new social and economic reality, that increasingly we are one Island community with one Island future. My Government is calling upon Islanders to recognize that Prince Edward***

***Island is a single community of interest, where essential services like health care and education are provided according to regional and provincial needs, and where there must be efficient and reasonable utilization of resources if all Islanders, regardless of where they live, are to be served equitably. We simply cannot afford to do otherwise".***

This statement of government policy is underlined in the Province's Island Prosperity Strategy. It is part of the overall intent of the Province to help the provincial economy claim its rightful place in a changing world. The new society envisioned will require strong and independent municipal units to create the living environment necessary to implement the Island Prosperity Strategy. Ensuring that the Capital Region Municipalities are capable of fulfilling their respective roles in the "one Island community" envisioned in the 2008 Throne Speech and in the Island Prosperity Strategy ought to be seen by both orders of government as being of paramount importance.

On behalf of the Consulting Team (MRS&A, Dr. Enid Slack and Kenneth F. DesRoches),

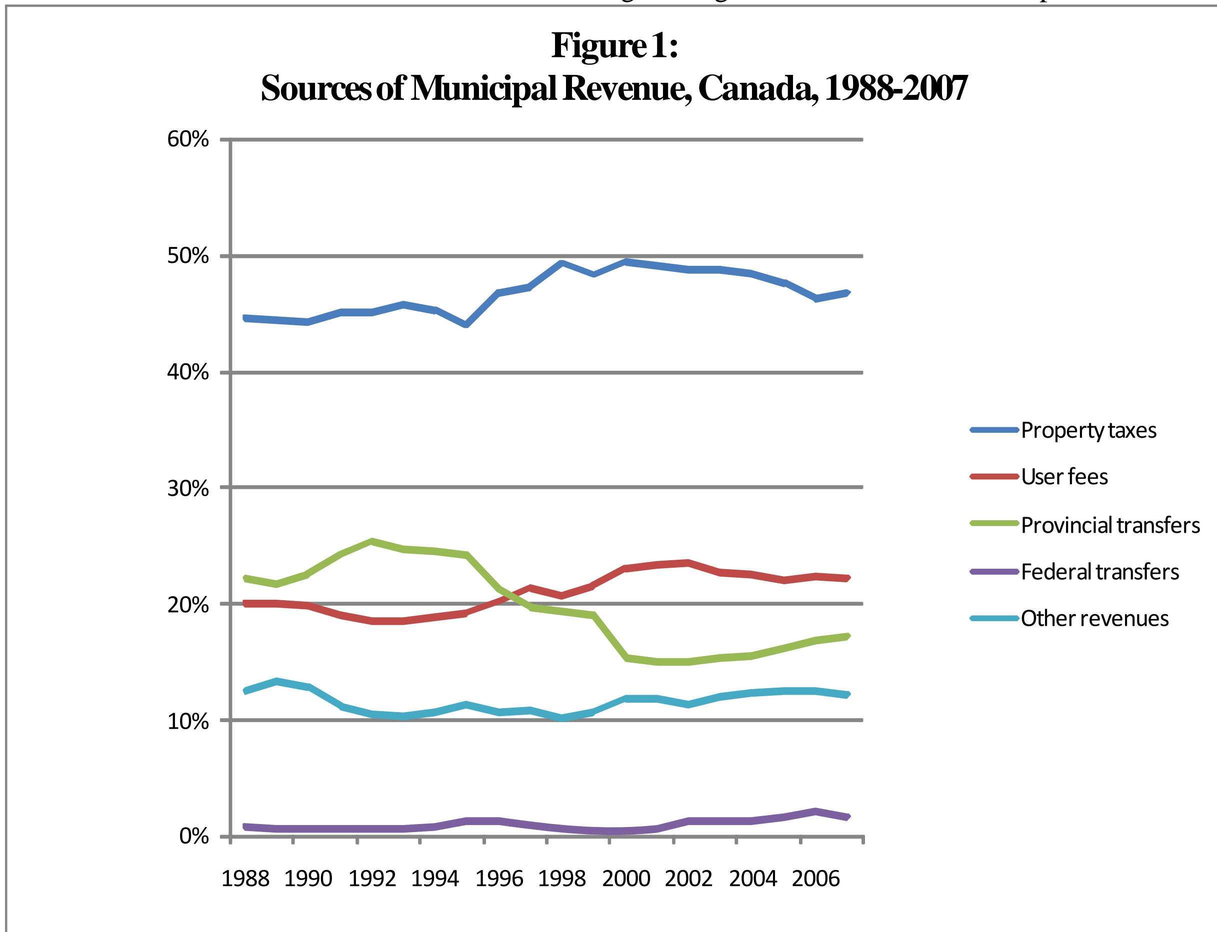
Respectfully submitted,

Stan H. MacPherson, FCA
Partner
MACPHERSON ROCHE SMITH & ASSOCIATES

November 20, 2008

# Appendix A

Source: Statistics Canada. Table 385-0024 – Local general government revenue and expenditures,




current and capital accounts, CANISM.

# Cornwall

**Impact of 2008 Budget Changes on Equalization Payments**

**Equalization formula:**

$$A/100 \times B \times (C/D - E/B)$$

*Where:*

**A** = the municipality's non-commercial property tax rate
**B** = the municipality's population
**C** = the provincial property tax assessment[1,2]
**D** = the total provincial population[1]
**E** = the municipality's property tax assessment[2]

[1] "provincial" only refers to incorporated municipalities
[2] "property tax assessment" includes both the commercial and non-commercial assessment

| | | Before 2008 Budget | Before Change To Grant System | After Change To Grant System |
|---|---|---|---|---|
| A | Non-commerical property tax rate | | $ 0.66 | $ 0.46 |
| B | Population | | 4,677 | 4,677 |
| C | Provincial assessment | | $ 5,371,575,366 | $ 5,371,575,366 |
| D | Provincial population | | 93,045 | 93,045 |
| E | Municipal assessment | | $ 220,348,400 | $ 220,348,400 |
| **Equalization Grant** | | $ 58,240 | $ 327,751 | $ 228,432 |

*Note: All figures used are based on approximations as provided by the municipalities*

APPENDIX C-1

# Charlottetown

**Comparison of projected value of tax credit vs. grant (using 10 years)**

| Year | Assessment | Growth |
|---|---|---|
| 1998 | $ 978,377,300 | 1% |
| 1999 | $ 999,532,300 | 2% |
| 2000 | $ 1,005,249,800 | 1% |
| 2001 | $ 1,045,917,900 | 4% |
| 2002 | $ 1,056,357,500 | 1% |
| 2003 | $ 1,160,657,500 | 10% |
| 2004 | $ 1,242,210,200 | 7% |
| 2005 | $ 1,359,934,200 | 9% |
| 2006 | $ 1,478,152,500 | 9% |
| 2007 | $ 1,595,040,608 | 8% |

| | |
|---|---|
| Average residential assessment growth, 1998-2007 | 5.2% |
| CPI, PEI, 1998-2007 | 2.6% |
| Tax credit rate | $ 0.66 |
| Residential assessment (2008) | $ 1,637,865,908 |
| Grant (2008) | $ 10,801,408 |

Projection

| Year | Residential Assessment | Tax Credit Value | Supplementary Cusa | Total CUSA | Grant Value | Difference |
|---|---|---|---|---|---|---|
| 2009 | $ 1,723,379,870 | $ 11,374,307 | $ 1,000,000 | $ 12,374,307 | $ 11,083,132 | $ 1,291,175 |
| 2010 | $ 1,813,358,567 | $ 11,968,167 | $ 1,000,000 | $ 12,968,167 | $ 11,372,203 | $ 1,595,963 |
| 2011 | $ 1,908,035,107 | $ 12,593,032 | $ 1,000,000 | $ 13,593,032 | $ 11,668,815 | $ 1,924,217 |
| 2012 | $ 2,007,654,765 | $ 13,250,521 | $ 1,000,000 | $ 14,250,521 | $ 11,973,162 | $ 2,277,359 |
| 2013 | $ 2,112,475,625 | $ 13,942,339 | $ 1,000,000 | $ 14,942,339 | $ 12,285,448 | $ 2,656,891 |
| 2014 | $ 2,222,769,245 | $ 14,670,277 | $ 1,000,000 | $ 15,670,277 | $ 12,605,879 | $ 3,064,398 |
| 2015 | $ 2,338,821,362 | $ 15,436,221 | $ 1,000,000 | $ 16,436,221 | $ 12,934,667 | $ 3,501,554 |
| 2016 | $ 2,460,932,629 | $ 16,242,155 | $ 1,000,000 | $ 17,242,155 | $ 13,272,030 | $ 3,970,125 |
| 2017 | $ 2,589,419,398 | $ 17,090,168 | $ 1,000,000 | $ 18,090,168 | $ 13,618,193 | $ 4,471,975 |
| 2018 | $ 2,724,614,539 | $ 17,982,456 | $ 1,000,000 | $ 18,982,456 | $ 13,973,385 | $ 5,009,071 |
| | | **$ 144,549,643** | **$ 10,000,000** | **$ 154,549,643** | **$ 124,786,914** | **$ 29,762,730** |

# Stratford

**Comparison of projected value of tax credit vs. grant (using 10 years)**

| Year | Assessment | Growth |
|---|---|---|
| 1998 | $ 195,517,276 | 4% |
| 1999 | $ 199,611,444 | 2% |
| 2000 | $ 224,622,008 | 13% |
| 2001 | $ 237,261,920 | 6% |
| 2002 | $ 255,665,581 | 8% |
| 2003 | $ 278,583,887 | 9% |
| 2004 | $ 298,423,421 | 7% |
| 2005 | $ 332,293,171 | 11% |
| 2006 | $ 386,255,762 | 16% |
| 2007 | $ 429,425,482 | 11% |

| | |
|---|---|
| Average residential assessment growth, 1998-2007 | 8.7% |
| CPI, PEI, 1998-2007 | 2.6% |
| Tax credit rate | $ 0.20 |
| Residential assessment (2008) | $ 450,757,782 |
| Grant (2008) | $ 901,516 |

Projection

| Year | Residential Assessment | Tax Credit Value | Grant Value | Difference |
|---|---|---|---|---|
| 2009 | $ 489,928,044 | $ 979,856 | $ 925,029 | $ 54,827 |
| 2010 | $ 532,502,150 | $ 1,065,004 | $ 949,156 | $ 115,848 |
| 2011 | $ 578,775,890 | $ 1,157,552 | $ 973,912 | $ 183,640 |
| 2012 | $ 629,070,758 | $ 1,258,142 | $ 999,314 | $ 258,828 |
| 2013 | $ 683,736,184 | $ 1,367,472 | $ 1,025,378 | $ 342,094 |
| 2014 | $ 743,151,964 | $ 1,486,304 | $ 1,052,122 | $ 434,182 |
| 2015 | $ 807,730,898 | $ 1,615,462 | $ 1,079,564 | $ 535,898 |
| 2016 | $ 877,921,657 | $ 1,755,843 | $ 1,107,721 | $ 648,122 |
| 2017 | $ 954,211,901 | $ 1,908,424 | $ 1,136,613 | $ 771,811 |
| 2018 | $ 1,037,131,667 | $ 2,074,263 | $ 1,166,258 | $ 908,005 |
| | | **$14,668,322** | **$ 10,415,068** | **$ 4,253,254** |

APPENDIX C-3

# Cornwall

**Comparison of projected value of tax credit vs. grant (using 10 years)**

| Year | Assessment | Growth |
|---|---|---|
| 1998 | $ 106,215,000 | 5% |
| 1999 | $ 110,878,166 | 4% |
| 2000 | $ 120,374,800 | 9% |
| 2001 | $ 125,999,300 | 5% |
| 2002 | $ 132,885,700 | 5% |
| 2003 | $ 145,213,700 | 9% |
| 2004 | $ 159,272,900 | 10% |
| 2005 | $ 175,797,500 | 10% |
| 2006 | $ 194,265,500 | 11% |
| 2007 | $ 210,686,700 | 8% |

| | |
|---|---|
| Average residential assessment growth, 1998-2007 | 7.6% |
| CPI, PEI, 1998-2007 | 2.6% |
| Tax credit rate | $ 0.20 |
| Residential assessment (2008) | $ 216,038,300 |
| Grant (2008) | $ 432,789 |

Projection

| Year | Residential Assessment | Tax Credit Value | Grant Value | Difference |
|---|---|---|---|---|
| 2009 | $ 232,525,716 | $ 465,051 | $ 444,077 | $ 20,974 |
| 2010 | $ 250,271,404 | $ 500,543 | $ 455,660 | $ 44,883 |
| 2011 | $ 269,371,391 | $ 538,743 | $ 467,544 | $ 71,199 |
| 2012 | $ 289,929,033 | $ 579,858 | $ 479,739 | $ 100,119 |
| 2013 | $ 312,055,576 | $ 624,111 | $ 492,251 | $ 131,860 |
| 2014 | $ 335,870,751 | $ 671,742 | $ 505,090 | $ 166,651 |
| 2015 | $ 361,503,432 | $ 723,007 | $ 518,264 | $ 204,743 |
| 2016 | $ 389,092,325 | $ 778,185 | $ 531,781 | $ 246,403 |
| 2017 | $ 418,786,722 | $ 837,573 | $ 545,651 | $ 291,922 |
| 2018 | $ 450,747,309 | $ 901,495 | $ 559,883 | $ 341,611 |
| | | **$ 6,620,307** | **$ 4,999,941** | **$ 1,620,366** |

# Charlottetown

## Projected Impact on Municipal Tax Rate

| Year | Tax Credit System | | | Grant System | | |
|---|---|---|---|---|---|---|
| | Residential Real Property Assessment | Provincial Tax Credit Rate | Provincial Tax Credit Value | Prior Year CPI Growth | Grant Value | Difference |
| 1998 | $ 978,377,300 | $ 0.66 | **$ 6,457,290** | 1.2% | **$ 6,457,290** | $ - |
| 1999 | $ 999,532,300 | $ 0.66 | $ 6,596,913 | -0.4% | $ 6,428,749 | $ (168,164) |
| 2000 | $ 1,005,249,800 | $ 0.66 | $ 6,634,649 | 1.2% | $ 6,507,236 | $ (127,413) |
| 2001 | $ 1,045,917,900 | $ 0.66 | $ 6,903,058 | 4.1% | $ 6,771,236 | $ (131,822) |
| 2002 | $ 1,056,357,500 | $ 0.66 | $ 6,971,960 | 2.6% | $ 6,949,614 | $ (22,346) |
| 2003 | $ 1,160,657,500 | $ 0.66 | $ 7,660,340 | 2.7% | $ 7,135,127 | $ (525,213) |
| 2004 | $ 1,242,210,200 | $ 0.66 | $ 8,198,587 | 3.5% | $ 7,384,857 | $ (813,730) |
| 2005 | $ 1,359,934,200 | $ 0.66 | $ 8,975,566 | 2.2% | $ 7,548,964 | $ (1,426,602) |
| 2006 | $ 1,478,152,500 | $ 0.66 | $ 9,755,807 | 3.1% | $ 7,784,424 | $ (1,971,383) |
| 2007 | $ 1,595,040,608 | $ 0.66 | $ 10,527,268 | 2.3% | $ 7,962,802 | $ (2,564,466) |
| 2008 | $ 1,637,865,908 | $ 0.66 | $ 10,809,915 | 1.8% | $ 8,105,504 | $ (2,704,411) |
| **10 Year Cumulative** | | | **$ 83,034,063** | | **$ 72,578,513** | **$ (10,455,550)** |

Assumptions

Assuming 1998 as the base year in which the new grant system was introduced and the grant was set as an amount equivalent to the 1998 tax credit. Compare the actual tax credit revenue of the 10 year period from 1999-2008 to the grant revenue for the same period assuming that the grant grew by CPI every year and calculate the actual effect that such a change would have had to this point in time. Assume annual revenue short-fall is recovered by increases to Municipal tax rates.

Projected Impact

The shortfall in 2008 of $2,704,411 amounts to $0.17 per $100 of assessment. This would mean that to provide the same level of service in 2008, rates would have had to been increased by $0.17 per $100. On a typical home assessed at $200,000, this would amount to an extra $340 of Municipal taxes per year, an increase of 13%.

# Stratford

## Projected Impact on Municipal Tax Rate

| Year | Tax Credit System | | | Grant System | | |
|---|---|---|---|---|---|---|
| | Residential Real Property Assessment | Provincial Tax Credit Rate | Provincial Tax Credit Value | Prior Year CPI Growth | Grant Value | Difference |
| 1998 | $ 195,517,276 | $ 0.20 | **$ 391,035** | 1.2% | **$ 391,035** | $ - |
| 1999 | $ 199,611,444 | $ 0.20 | $ 399,223 | -0.4% | $ 389,307 | $ (9,916) |
| 2000 | $ 224,622,008 | $ 0.20 | $ 449,244 | 1.2% | $ 394,060 | $ (55,184) |
| 2001 | $ 237,261,920 | $ 0.20 | $ 474,524 | 4.1% | $ 410,047 | $ (64,477) |
| 2002 | $ 255,665,581 | $ 0.20 | $ 511,331 | 2.6% | $ 420,849 | $ (90,482) |
| 2003 | $ 278,583,887 | $ 0.20 | $ 557,168 | 2.7% | $ 432,083 | $ (125,085) |
| 2004 | $ 298,423,421 | $ 0.20 | $ 596,847 | 3.5% | $ 447,206 | $ (149,641) |
| 2005 | $ 332,293,171 | $ 0.20 | $ 664,586 | 2.2% | $ 457,144 | $ (207,442) |
| 2006 | $ 386,255,762 | $ 0.20 | $ 772,512 | 3.1% | $ 471,402 | $ (301,110) |
| 2007 | $ 429,425,482 | $ 0.20 | $ 858,851 | 2.3% | $ 482,204 | $ (376,647) |
| 2008 | $ 450,757,782 | $ 0.20 | $ 901,516 | 1.8% | $ 490,846 | $ (410,670) |
| **10 Year Cumulative** | | | **$ 6,185,802** | | **$ 4,395,147** | **$ (1,790,655)** |

Assumptions

Assuming 1998 as the base year in which the new grant system was introduced and the grant was set as an amount equivalent to the 1998 tax credit. Compare the actual tax credit revenue of the 10 year period from 1999-2008 to the grant revenue for the same period assuming that the grant grew by CPI every year and calculate the actual effect that such a change would have had to this point in time. Assume annual revenue short-fall is recovered by increases to Municipal tax rates.

Projected Impact

The shortfall in 2008 of $410,670 amounts to $0.09 per $100 of assessment. This would mean that to provide the same level of service in 2008, rates would have had to been increased by $0.09 per $100. On a typical home assessed at $200,000, this would amount to an extra $180 of Municipal taxes per year, an increase of 14%.

APPENDIX D-3

# Cornwall

## Projected Impact on Municipal Tax Rate

| Year | Tax Credit System | | | Grant System | | |
|---|---|---|---|---|---|---|
| | Residential Real Property Assessment | Provincial Tax Credit Rate | Provincial Tax Credit Value | Prior Year CPI Growth | Grant Value | Difference |
| 1998 | $ 106,215,000 | $ 0.20 | **$ 212,430** | 1.2% | **$ 212,430** | $ - |
| 1999 | $ 110,878,166 | $ 0.20 | $ 221,756 | -0.4% | $ 211,491 | $ (10,265) |
| 2000 | $ 120,374,800 | $ 0.20 | $ 240,750 | 1.2% | $ 214,073 | $ (26,677) |
| 2001 | $ 125,999,300 | $ 0.20 | $ 251,999 | 4.1% | $ 222,758 | $ (29,241) |
| 2002 | $ 132,885,700 | $ 0.20 | $ 265,771 | 2.6% | $ 228,626 | $ (37,145) |
| 2003 | $ 145,213,700 | $ 0.20 | $ 290,427 | 2.7% | $ 234,729 | $ (55,698) |
| 2004 | $ 159,272,900 | $ 0.20 | $ 318,546 | 3.5% | $ 242,945 | $ (75,601) |
| 2005 | $ 175,797,500 | $ 0.20 | $ 351,595 | 2.2% | $ 248,344 | $ (103,251) |
| 2006 | $ 194,265,500 | $ 0.20 | $ 388,531 | 3.1% | $ 256,090 | $ (132,441) |
| 2007 | $ 210,686,700 | $ 0.20 | $ 421,373 | 2.3% | $ 261,958 | $ (159,415) |
| 2008 | $ 216,038,300 | $ 0.20 | $ 432,077 | 1.8% | $ 266,652 | $ (165,425) |
| **10 Year Cumulative** | | | **$ 3,182,825** | | **$ 2,387,666** | **$ (795,159)** |

Assumptions

Assuming 1998 as the base year in which the new grant system was introduced and the grant was set as an amount equivalent to the 1998 tax credit. Compare the actual tax credit revenue of the 10 year period from 1999-2008 to the grant revenue for the same period assuming that the grant grew by CPI every year and calculate the actual effect that such a change would have had to this point in time. Assume annual revenue short-fall is recovered by increases to Municipal tax rates.

Projected Impact

The shortfall in 2008 of $165,425 amounts to $0.08 per $100 of assessment. This would mean that to provide the same level of service in 2008, rates would have had to been increased by $0.08 per $100. On a typical home assessed at $200,000, this would amount to an extra $160 of Municipal taxes per year, an increase of 12%.