



# CIVIC AFFAIRS

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## PROVINCIAL-MUNICIPAL RELATIONS WITH EMPHASIS ON THE FINANCIAL RELATIONS BETWEEN PROVINCES AND LOCAL GOVERNMENTS

*(A speech given by the Director, Eric Hardy, at the Eleventh Annual Conference of The Institute of Public Administration of Canada in the Royal York Hotel, Toronto, Ontario, October 24, 1959)*

In view of the dominant position occupied by the provinces in Provincial-Municipal Relations, and the exposed financial position of the municipalities, it may be questioned whether the provinces are giving the municipalities the best possible leadership towards the solution of today's problems. Some basic factors in the system need examination, and certain shortcomings in the performances of both provinces and municipalities call for attention.

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### THE PROVINCE IS IN COMMAND

I have been asked to present a factual paper on provincial-municipal relations which is intended to set the stage for a general discussion. It is no mean task. In order to encompass the subject in any reasonable manner, it seems essential to select some particular aspect of the theme and to direct my remarks accordingly. I have decided, therefore, to emphasize the financial relationships between these two levels of government. What is more, I have no intention of attempting to document each point. You will have to judge from your own experience whether or not the coverage is reasonably balanced and factual.

As I see it, the very term provincial-municipal relations is apt to mislead us as to the nature of this relationship. People are all too ready to draw a parallel with Dominion-provincial relations where the contacts are between two sovereign levels of government which are relatively independent of one another. In 1940 and again in 1945, Dominion-provincial conferences collapsed because the two levels of government disagreed on fundamentals and neither side had the power to force agreement. By contrast, a provincial government which is sure of its ground can require its local governments to accept its proposals. If they are not adopted at the conference table, they can be imposed by legislation.

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Provincial - municipal relations are not unlike the relationship between a parent company and its wholly-owned subsidiaries. Originally, the province enabled local governments to be formed. The province has provided for the overall system of local government within its boundaries, including the broad form of organization of municipal corporations and associated local boards, the status of various classes of municipalities and the broad powers and responsibilities of all local governments.

The relative standing of provinces and municipalities is less evident today than it used to be because responsibilities for particular services tend to involve an increasing number of provincial-municipal partnership arrangements. An important feature of most such arrangements is the development of shared cost programmes which become the vehicle for dividing not only the financial burden but the policy control and administrative responsibilities.

But compare the introduction of Dominion-provincial and provincial-municipal shared cost programmes.

When the Government of Canada offers grants to the provinces with strings attached, its hope is that the financial terms may be sufficiently enticing to ensure that all or most provinces accept the total proposal including conditions as to how the money is to be spent.

A province is quite free to forego the financial assistance and thereby reject the attempted control over the form, extent or quality of the service.

When a provincial government offers conditional aid, it is wearing the velvet glove. But if this approach is not fully successful, the province can show the iron hand. As one instance, the Province of Ontario now requires its municipalities to fit into the shared cost arrangements for unemployment relief and to provide such relief according to the province's rules.

The courtesy and forbearance which is common in provincial-municipal relations should not blind us to the essential master-servant relationship. Let me illustrate further.

In every province of Canada, incorporated municipalities are required to employ the real property tax as their principal and residual form of local revenue raising. Moreover, provincial statutes prescribe how real property is to be assessed in order to form a suitable base for property taxes. Again, with one minor exception, the provinces have stripped local governments of the power they formerly enjoyed to levy corporate and personal income taxes. In spite of the loss of these lucrative forms of taxation, few new tax sources have been made available. In only one province, Quebec, has the retail sales tax been allowed to become a municipal levy. In only two provinces, Saskatchewan and Newfoundland, can the municipalities impose the amusement tax, although in a third, Quebec, the revenues from this source are by statutory arrangement divided between the province and its municipalities.

It is well to remember, also, that the provinces have established a form of government for municipalities and school boards which differs in essentials from their own systems. Municipalities and school boards have nothing which corresponds to a cabinet or to government by the party in power. Again, members of local councils and school boards are elected for definite terms of one, two or three years whereas provincial legislators are given a maximum term which permits choosing a strategic moment for the next election.

Such differences in no small way affect the budget process. In local government each annual budget is measurably close to the next election. Each item in the budget must command majority support but no group of representatives and often no single representative becomes committed to the support of the entire budget. Add to that the fact that the estimates are prepared and adopted in the home community and we can see why the municipal budget is normally subjected to so much sniping both from inside and outside the council.

At the level of the appointed officials, we find another example of the province's dominant position. Municipalities in all parts of Canada must appoint a number of statutory officers whose important duties are spelled out in detail in provincial legislation. Among others, municipalities are usually required to appoint treasurers, tax collectors, assessors and auditors. These officials must satisfy the statutory requirements of their offices and attempt at the same time to serve the wishes of their local councils. Where the two objectives conflict, the provincial responsibility takes precedence.

Finally, the province directs local governments to provide certain services, whereas, on its part, the province has the power to provide services but no requirement to do so beyond the necessary response to the demands of its public. Education was among the earliest of the compulsory local government services. Public health has become another. Specified welfare functions such as children's aid and care of the aged have commonly been made mandatory. In urban municipalities, policing is usually a compulsory local government undertaking.

In practice, there is a tendency for the distinction between mandatory and permissive local government functions to disappear. For one thing, conditional grants have been employed as a means of pressuring municipalities into providing so-called optional services which are considered necessary in the public interest. The police and fire grants which were paid by Ontario for a period of six years until they were discontinued in 1954, were intended to bring about the performance of satisfactory policing and fire protection in all urban municipalities where these services were needed. But even without such persuasion, the municipalities have no choice but to provide most of the permissive services. Once the responsibility has been clearly allocated to local government, the necessity of making the service available becomes patent because of public demand for it. In essence, therefore, the character and extent of local government undertakings are fairly clearly defined as a result of the provinces' power to designate local government services and to ensure that the important undertakings are, in fact, carried out on a reasonably satisfactory level.

### MUNICIPALITIES ARE FINANCIALLY VULNERABLE

The province's expectation that its local governments will furnish certain services implies a corresponding responsibility to make sources of revenue available to them. Yet this fact does not ensure that the permitted methods of revenue raising will be appropriate to the purposes to be served or sufficiently generous to enable the money to be raised without tax hardship.

In recent years local governments have contended that their available revenue sources were both inadequate and unsuitable. The response from the provinces has been two-fold — to launch a number of enquiries into the subject by Royal Commissions or similar bodies; and to bolster the local treasuries through increased grants-in-aid and the declaration of some shared taxes. Between the fiscal years ending March 31, 1947 and 1957, annual transfers from the provinces to their municipalities jumped from \$95 million to \$361 million. In other words, the total nearly tripled.

Local governments are not yet satisfied. In the absence of new tax sources which the provinces seem unwilling or unable to make available, some people have proposed that certain functions of local governments be taken over by the provinces. For example, it has been suggested that the remaining obligations for administration of justice in the central and Maritime

provinces should be removed from the municipalities' shoulders. In the three most westerly provinces local governments have no responsibilities in this field.

A more common form of suggestion — although less reasonable — has been that the provinces should finance all or all but a token portion of the cost of particular services of wider than local concern, notably education and social services, without, however, altering the legal jurisdiction.

#### HOW PROVINCIAL-MUNICIPAL RELATIONS ARE CONDUCTED

Next, let us take a brief look at the form of the relationship between the province and its local governments.

When a municipality approaches the province on any question of genuine importance it is normally represented by one or more elected representatives, perhaps with the support of appointed officials. The local delegation customarily finds, however, that it deals with appointed officials at the provincial level. There may be discussions in which the appropriate Minister is present. But that is not the expected pattern in most instances. In other words, in financial as in other matters the customary choice of spokesmen emphasizes the dominant position of the province in provincial-municipal relations.

When a local government problem concerns roads, the municipality deals directly with the Department of Highways; when the subject is public health, with the Department of Health; on school matters, with the Department of Education and so on. Indeed, virtually every department of the provincial government has direct dealings with local governments. And with few exceptions the individual departments also have direct financial relationships with the local authorities.

There is at least a partial reason, historically, for this lack of centralization in provincial-municipal relations. In five Canadian provinces, departments of municipal affairs are Johnnies-come-lately. Four of them were created in the depression years and one more recently. In Quebec and the three Prairie Provinces, corresponding departments date back much earlier and they appear to occupy a stronger position accordingly. While Prince Edward Island has not yet seen fit to set up a department of municipal affairs, there is not for a number of reasons the average urgency to do so.

Even in Quebec and the Prairie Provinces, departments of municipal affairs have not been given clear seniority over other departments in the relationship with local governments. Moreover, it is open to question whether departments of municipal affairs are kept fully informed on all business which other departments are transacting with local governments.

The fact that in most provinces all major departments of government have direct dealings with local governments has influenced the system of grants and payments to municipalities, local school boards and other special purpose bodies. The money is most frequently forthcoming in the form of conditional grants to assist particular services. The provincial department

which is responsible for the corresponding services determines or helps to determine the grant formula. It clings to the conditional grant because it can thereby take its share of credit for resulting accomplishments. For example, a provincial welfare department can boast of the help it is providing to the needy through public assistance programmes which are operated by local authorities on its terms and with its financial aid.

If, in each province, the department of municipal affairs was the sole department permitted to subsidize local governments, several differences might be anticipated from the situation today. The variety of formulas for calculating conditional grants would probably be cut down. The number of conditional grants would likely be reduced and the proportion of unconditional aid increased. A more comprehensive knowledge of local government operations would be accumulated in one place.

Two exceptions to the customary departmental breakdown of provincial-municipal transactions are important. The nine municipal affairs departments collect and publish municipal financial statistics embracing all major aspects of local government operations. More significant, a single authority is responsible for approving capital borrowing beyond the current year for all local government purposes. In the majority of provinces a semi-judicial body carries out this function. In others, it is the department of municipal affairs. In Newfoundland the Cabinet does the job. In New Brunswick, the responsibility is, I gather, divided by classes of municipalities. Cities and counties must obtain the assent of the provincial legislature, towns and villages secure their approvals through the department of municipal affairs. These centralized functions in the field of finance strengthen the co-ordination of provincial-municipal relations in their broader aspects.

#### CO-ORDINATION IN LOCAL GOVERNMENT

Local government throughout Canada is normally itself a house divided. Separate bodies with varying degrees of independence from the municipal corporation commonly exercise responsibility over such services as schooling, public utilities, policing, public libraries, parks, municipal hospital services, public welfare and so forth. Besides these divisions with respect to services performed within the boundaries of a single municipality, other special purpose bodies have been set up with jurisdiction embracing parts of two or more municipalities. Examples include larger school districts, health units, hospital districts, road commissions and conservation authorities.

The closest tie between the municipal corporation and such associated local boards lies in the field of finance. Many such bodies obtain the bulk of their current revenues from taxation by the municipality proper. And yet municipalities tend to view the financial operations of such boards and commissions as outside their field of responsibility. In Manitoba, for example, it is customary in the municipal audits to describe such payments officially as "uncontrollable expenditures". Similarly, there is perhaps an increasing tendency for

the province to by-pass the municipal corporation in making conditional grants in support of services coming under a special purpose body. In illustration, Ontario's Department of Welfare used to route its grants to homes for the aged through the responsible county, city or town but now makes the payment directly to the board of the home.

On capital borrowing, the role of the municipal council is stronger still. Generally speaking, special purpose bodies must ask the municipal corporation to issue debentures on their behalf. School corporations within the Province of Quebec and in parts of western Canada constitute an important exception; they enter the market for their own requirements and need not obtain the municipality's permission to borrow. Similarly, school boards in unorganized territories and separate school boards borrow on their own.

### THE EXTENT OF LOCAL AUTONOMY

In what I have said so far, the dependent position of local government in provincial-municipal relations has been stressed. I have spelled out this side of the story believing it is commonly under-emphasized in present-day discussions and sometimes completely overlooked. But the other view of the relationship — which stresses local autonomy — is also significant and, indeed, creates the usual climate for provincial-municipal discussions. Let me add, too, that it contributes to some of our thorniest present-day problems.

Local governments are not intended to be mere agencies of the province. They gained rights of local self-government in pioneer days and have worked hard to maintain the tradition. One indicator of municipal status today is the importance municipal and school associations have attained in gathering and putting before the province in terms of both law and practice the views of local authorities on provincial-municipal relations. Whether the associations have official standing or not, no province consistently ignores what they have to say.

As I see it, local governments have the right to expect that they will remain responsible for a major share of public services, that they will be given access to public revenue sources sufficient to finance such services, and that they will retain a reasonable amount of choice and of freedom from interference in the conduct of their operations. That is my definition of local autonomy.

In many respects local governments enjoy the autonomy to which they are entitled. They retain a good deal of freedom of action in the day-to-day operations of municipal services. The character of many local government services is determined primarily by the wishes of the local citizenry. In areas where it is still appropriate, local governments can decide whether or not to embark upon particular service undertakings. The amount of public housing, for example, is decided by local option. Perhaps this results in less activity in this field than many people would like. Nevertheless, considering the generous subsidies available from senior

governments, the combined performance across Canada probably reflects quite closely the attitudes of the Canadian people.

### DO THE PROVINCES GIVE LEADERSHIP?

It is said repeatedly that the local level of government offers an excellent and perhaps the best field for experimentation; and probably this is true. Local government has produced variety in the forms of governmental organization and in methods of administration. It has introduced new public services on a trial basis and has tested new forms of revenue raising. The retail sales tax was pioneered in Canada by the City of Montreal and its suburbs. Then the Province of Quebec moved into the field and five other provinces have followed suit. Locally, this tax is now employed by most municipalities and school corporations throughout Quebec Province.

I sometimes wonder, however, if the provinces are not too eager to permit local experimentation and too reticent in examining and passing an opinion on what happens.

The traditional view of licensing has been that the businesses, persons or things to be licensed should be limited to those requiring government regulation, inspection or similar supervision and that the license fee should be no more than is required to meet the cost of such services. Today, however, in their scramble for additional revenues, municipalities are sometimes applying licensing where no supervision appears to be called for and are frequently imposing fees which constitute hidden taxation, and not very well hidden at that. Is such a method of revenue-raising likely to prove equitable in practice and to fit reasonably well into the overall pattern of taxation?

Let me give you a further illustration. Legislation permitting municipalities to levy poll taxes has remained on the statute books for many years although the justification for this form of revenue raising has become increasingly dubious. Certainly to confine the tax to males as is done in Ontario and Quebec makes little sense. Again, what is the logic in charging roomers but exempting tenants on the theory that they pay taxes indirectly through rent? Finally, where a property franchise still exists, is it not taxation without representation to impose a poll tax on other adult residents?

The provinces have not merely been passive observers of this out-dated type of tax. In the Maritime Provinces, they have permitted the field to be opened wider so that poll taxes of fifteen, twenty or twenty-five dollars per annum are common.

One may well ask whether the provinces are converting the tradition of local autonomy into an excuse to shirk their leadership responsibilities. Municipalities are quite capable of carrying out experiments in government but less well equipped to assess the results. Should the provinces not regard this as a part of their responsibility in provincial-municipal relations?

## MUNICIPAL BOUNDARIES AND REVENUE INEQUITIES

In no aspect of government has the tradition of local autonomy been more firmly rooted than in the provinces' position on local boundary questions. Local government is the one level of government which must accommodate itself continually to changes in the population and character of communities. A century ago, the municipalities concerned could be counted upon to seek the changes required by both rural and urban expansion. Legislation was framed accordingly.

Today the explosive rate of growth and the extent of urban scatteration has altered the position completely. It is now an old story. Technological changes have brought the mass use of the automobile, the shorter working day and work week, rural electrification, year-round roads and so on. They have enabled people to live further from where they work and even factories and shopping centres to migrate to the country.

Those who have any serious contact with government are becoming increasingly familiar, also, with the repercussions upon municipal financing from failure to effect needed boundary adjustments.

Where the community is purely rural or very largely so, small units of government are unable to take advantage of modern equipment or to achieve standards in the social services which can be reached by a government embracing a large constituency. Such small units also involve sharp inequalities in the financial strength of individual rural municipalities which could readily be eliminated by pooling the cost of government over wider areas.

In urban communities or areas where urban dwellers are invading the farmlands, we encounter a different problem. In a farm property, the residential and business uses are both recognized in a single assessment for tax purposes. In urban communities the assessment is split between residential and business holdings. Where a balanced urban community is contained within the boundaries of a single municipality, and a standard pattern of taxation and a normal complement of services are provided we find that residential properties draw down more in services than they yield in tax revenues, while for business properties the position is reversed.

As part of a statistical service, our Citizens Research Institute asks municipalities to report the percentages of their total assessments which are attributable to business properties. I have sorted the returns from sixty-two municipalities of 10,000 population and over to give you some idea of the situation which exists today. The selection is entirely random and the tabulation may not present an entirely fair picture. But the figures give us something to think about.

We might expect a business content of between thirty and fifty per cent in a municipality whose assortment of properties is reasonably balanced. Twenty-nine municipalities were included in this group. Twenty-seven municipalities reported less than thirty per cent of their total assessments against business and of this number no less than twelve had less than ten per cent. On the

other end of the scale, there were six municipalities with more than fifty per cent in business assessments and one of these was in the eighty to ninety per cent range.

From various quarters the suggestion is being made that we will have to pool the revenues from taxation of business properties over wider areas than single municipalities unless a drastic enlargement of urban boundaries can somehow be accomplished. In addition to our own organization, the idea was advanced by one of the speakers at a recent conference of the Canadian Federation of Mayors and Municipalities. It was considered again by the Province of Alberta in looking at the problem of the Edmonton and Calgary metropolitan areas and it has recently appeared in one of the recommendations of the Greater Winnipeg Investigating Commission.

The full repercussions of the lack of balance in the tax base of many urban communities are being postponed in many municipalities by the method which is being used to finance the opening up of new subdivisions. Where the entire cost used to be met from the general rate, local improvement levies are being introduced. Where local improvement levies have been in practice much of the cost or even the entire cost is being thrown upon the subdivider or developer. When financed in this way, the original expenditures for roads and sidewalks, sewer and water, street lighting and even school accommodation may not get into the tax picture at all but be paid instead in the form of a higher purchase price and probably a larger mortgage by the home buyer. Consequently, in the municipal accounting, a new subdivision can prove profitable to a municipality. But in the long run it will become like other residential areas a liability which can be quite embarrassing if there are not sufficient businesses within the municipality to produce the balancing revenues.

## PROVINCIAL REGULATION OF MUNICIPAL DEBT

May I take the time to cover one final point? Since the 'thirties, every province in Canada has supervised all local government borrowing activities which call for financing beyond the current year. The purpose for which the money is to be used and the capacity to pay the debt from some revenue-earning enterprise or from taxation is carefully scrutinized. It might appear that the provinces are going as far as they should and that the current increase in municipal indebtedness and likewise the inability of municipalities to borrow at modest interest rates or in some cases to borrow at any sensible figure merits their sympathy but nothing more. Actually, several provinces have gone further. Alberta, Ontario and Nova Scotia have operated revolving funds through which local governments can borrow from the province whether at normal or preferred interest rates. Saskatchewan has made a regular practice of buying up municipal debentures. British Columbia has guaranteed a large volume of local government debenture debt. The Province of Quebec has taken a somewhat different tack in twice absorbing outstanding debenture obligations of its school corporations.

I am not at all sure that this umbrella arrangement which facilitates borrowing without subjecting local governments to the test of the market is sound. Be that as it may, the question I raise is whether it is appropriate for local governments to rely to the limit on borrowed money as I believe many of them are in the process of doing.

By a rough calculation, Canadian municipalities are today committed in advance on about twenty per cent of their current budgets for debt charges. True, some of the money will be paid in by revenue-earning enterprises whose current income is not included in these same municipal budgets. But the position is not healthy. Undertakings which are financed through borrowing cost more than they otherwise would and an undue emphasis on borrowing reduces the financial capacity of a level of government which is already caught in a squeeze on current revenue sources.

Most commonly, provincial approvals of capital borrowing are treated as a semi-judicial process. Agencies like the Quebec Municipal Commission or the Ontario Municipal Board are supposed to base their decisions on the municipality's ability to borrow without considering whether it is prudent for it to do so. Where the screen-

ing of borrowing requirements is handled in this manner, has not the provincial government a further responsibility?

Devices have long been contained in provincial legislation which were presumably intended to meet this problem, notably the money by-law referendum and the statutory borrowing limit. As I see it, neither of these plans has proven fully satisfactory and indeed both are less widely required and used than formerly. Hence, my view that some different form of provincial control is called for.

In conclusion, I should like simply to say that local governments are encountering sufficient difficulties in both current and capital financing to warrant reconsideration of the fundamentals of provincial-municipal relations.

November 9, 1959