EXECUTIVE SUMMARY

FRASER INSTITUTE

Local Leviathans

The Rise of Municipal Government Spending in Canada, 1990–2018

by Livio Di Matteo

Canada's municipalities have increased their spending and employment over the last two decades while maintaining that they are fiscally challenged. Notwithstanding the recent pandemic-induced fiscal shocks, they typically run surpluses on their operating budgets while continuing to increase tax levies. Understanding municipal finance is important given the centrality of services such as roads, water, police and fire protection, and transit to Canadian families. At the same time, understanding municipal finances is a challenging exercise given they are not very transparent and vary widely across municipalities.

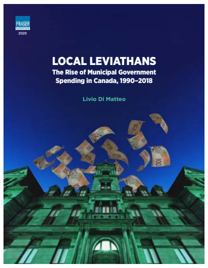
As municipalities typically run surpluses or balanced operating budgets, total revenues are an excellent indicator of their fiscal activity over time. Between 1991 and 2018, total real local government revenues in Canada grew from $107 billion to $186 billion—an increase of 74% while real per-capita total revenues have grown from $3,831 in 1991 to $5,024 in 2018—an increase of 31%. Total real property-tax revenue in 2018 dollars grew from $42.2 billion in 1991 to reach $71.7 billion by 2018—an increase of 70%. Meanwhile, revenue from government grants grew from $48.7 billion to $80 billion for an increase of 64%, while all other revenues grew 107%—from $16.6 billion to $34.4 billion. Thus, own-source revenues of one type or another saw the most robust growth.

Property taxes alone accounted for 48% of revenues, followed by another 8% in other miscellaneous local taxes. Government grants yielded another 19% of revenues, which was followed by 25% coming from all other revenues consisting of assorted fees from services like transit or housing, recreational activities, and other goods that vary across municipalities. The composition of major expenditures is revealing: 37% of operating expenses are in employee compensation, another 28% are from the purchase of goods and services to run municipal operations, and 20% are expenses associated with fixed capital-consumption costs.

The increase in operating spending is driven by several factors. Growing revenues from property taxes, intergovernmental grants, and the sales of goods and services are positively related to rising per-capita municipal expenditures. Essentially, one can argue that municipal spending rises to fill the revenues available. Moreover, on the cost side, increases in the number of municipal employees coupled with their pay rates is also a positive driver of rising municipal spending. This suggests that municipalities in Canada for the most part have been able to increase their spending because of a more than adequate ability to generate revenues to fuel that spending. The municipal wage rate and the number of municipal employees both are positive and significant determinants of per-capita municipal spending. As well, the size of the real per-capita municipal operating surplus is positively and significantly related to real per-capita property-tax revenues and real per-capita grant revenues.

Over the long term, municipalities have played an interesting game. They are required by provincial legislation not to run operating deficits and they have not only managed to balance their budgets but generate operating surpluses most years and potentially add to their reserves. Indeed, over the period from 2008 to 2018, the operating surplus for municipalities in Canada ranged from a low of 6.1% of revenues in 2014 to a high of 11.9% in 2017.

Given the significance of both municipal wage rates and employment numbers as positive drivers of spending and negative drivers of the operating surplus, it stands to reason that municipalities need to make more of an effort to address their spending. Only after such an effort, can it be reasonable for municipalities to request additional support from upper tiers of government or increased taxes from their own ratepayers. Municipal ratepayers and provincial and federal governments alike need to be cautious that the current COVID-19 crisis is not used by municipalities as simply an opportunity to finance a long-term enrichment of their spending.



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Municipal government spending and revenues up more than 50% across Canada from 2008 to 2018