

# **Structuring Federal Urban Engagement: A Principled Approach**

*A Western Cities Project Discussion Paper*

**Loleen Berdahl  
Director of Research**

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## Introduction

In recent years, growing attention has been paid to Canada's large cities. One particularly significant development has been the increased federal interest in cities. In May 2001, Prime Minister Chrétien appointed the Prime Minister's Caucus Task Force on Urban Issues to consult with Canadians and key urban stakeholders about a potential federal engagement in urban issues. The Task Force's interim report, released in April 2002, called for the creation of a federal "urban lens," as well as federal policy attention in key areas. The September 2002 Speech from the Throne argued that, "Competitive cities and healthy communities are vital to our individual and national well-being, and to Canada's ability to attract and retain talent and investment. ... They require new partnerships, a new urban strategy, a new approach to healthy communities for the 21st century" (Government of Canada 2002). Among the federal initiatives promised were a tripartite "ten-year program for infrastructure to accommodate long-term strategic initiatives essential to competitiveness and sustainable growth," "investments in affordable housing for those whose needs are greatest, particularly in those Canadian cities where the problem is most acute," a national drug strategy, and programs for homelessness, urban Aboriginal peoples, and immigrant settlement.

While the engagement of the national government in cities is not unheard of in federal systems, the Canadian federal government has a very limited history of federal-municipal relations (Berdahl and Sapergia 2001). The opportunity now exists to develop a urban strategy that benefits Canada's urban areas over the long-term. The danger also exists, however, for the creation of federal policies that undermine the long-term wellbeing of cities, damage federal-provincial and provincial-municipal relations, and serve nothing more than immediate federal interests. The challenge is to devise an urban strategy that is appropriate to the Canadian federal system, and to the needs of Canada's large cities.

The objectives of *Structuring Federal Urban Engagement* are to outline principles to guide federal urban policy, in light of the recent federal interest in cities. The paper will answer three sets of questions:

- What principles should guide federal engagement in cities? What are the risks if federal engagement fails to follow these principles? What would these principles mean on a practical level with respect to federal funding for cities?
- What steps could the federal government take to improve its awareness of the impact of federal policies on cities?
- How can federal, provincial and municipal governments work together cooperatively to ensure the long-term wellbeing of Canada's cities? What are some examples of policy tools that might be employed?

*Structuring Federal Urban Engagement* is analysis-based, and focuses on broad principles and intergovernmental dynamics rather than on specific policy recommendations. The research base for *Structuring Federal Urban Engagement* is the Canada West Foundation's *Western Cities Project*, since 1999, the *Western Cities Project* has produced over 20 innovative and authoritative studies in the areas of urban finance, urban governance, urban growth and affordable housing, urban Aboriginal peoples, and urban arts and culture, among other topics. (See [www.cwf.ca](http://www.cwf.ca) for a complete list of the research studies.) During the course of the project, the Canada West Foundation engaged or consulted over 600 urban experts and practitioners. What became clear during the *Western Cities Project* is that many urban challenges in western Canada (and, one might presume, Canada as a whole) are related to intergovernmental structures. *Structuring Federal Urban Engagement* represents a synthesis of Canada West's urban research as it pertains to intergovernmental relations.

### *Federal Engagement in Cities: A Principled Approach*

Seven principles should guide federal engagement in urban issues. These seven principles, along with their rationales and practical implications, are outlined below. As the discussion notes, there are considerable risks if these principles are not followed. It must also be stressed that these seven principles are interrelated, and in an ideal environment all seven would be followed.

#### **Principle #1: Local governments should identify local priorities; the federal government should be facilitative, not directive.**

Local government has the advantage of being closest to the people, both literally and in terms of public-government interaction. This closeness means that local governments are in the best position to identify their key urban policy priorities, both broadly (e.g., building new roads versus expanding the police force) and within policy fields (e.g., building a new interchange versus expanding a subway line). For this reason, municipal governments should have some formal mechanism for communicating these priorities to the federal government, and local priorities should be the focus of tripartite agreements. It is simply inappropriate for public servants or politicians in Ottawa to decide the policy priorities in Saskatoon, Montreal or Edmonton. This approach would result in the distortion of municipal funding priorities, a lack of innovation, and the erosion of local control.

On this point, lessons can be drawn from the American experience. Canadian policy debate often points to a more substantive (or at least more visible) federal urban engagement south of the border. What is less acknowledged is criticism of U.S. federal urban programs, which are seen as being "one-

size-fits-all” rather than targeted at the particular needs of individual cities, as well as over-bureaucratized and detrimental to local control (see, for example, Katz 2000).

There is reason to believe that the Canadian public would not support a federal role in cities that is directive in nature. Speaking of a Winnipeg roundtable, the Institute of Urban Studies writes, “Participants at the roundtable expressed clear support for a federal role in urban issues. But there was also a strongly held view that this role should not include setting the urban agenda or directing efforts to deal with urban issues. Participants felt that the most appropriate role for the federal government would be to support locally based and locally defined priorities, efforts and solutions. ... Boiler plate, one-size-fits-all federal programs were seen as more problematic than helpful” (2001, 11).

Federal engagement in cities must be *responsive* to municipal needs as expressed by municipal governments; federal *perception* of needs, even if generated by federal officers in locally based offices, is insufficient. The federal government’s role is to be facilitative, not directive. This will require considerable self-restraint on the part of the federal government, but can be achieved. For tripartite agreements, one model might be to give municipal governments responsibility for generating project ideas, and then have them approach the federal and provincial governments for partnership. The federal government could define broad funding categories (e.g., “infrastructure” or “environment”) and provide basic project criteria (e.g., “project should promote urban density/urban transit usage”), but leave the development of actual project ideas to municipal governments. This approach would limit the spending priority distortions typically associated with grant funding.

The federal government must also be open to the probability that local priorities may include much-needed repair or maintenance of existing infrastructure, in addition to the building of new infrastructure. While new projects have a greater deal of glamour than repair work, it may be the case that existing infrastructure represents the more critical strategic investment, and that building new infrastructure would only add to the city’s maintenance burden.

**Principle #2: Federal engagement in urban affairs should occur within a tripartite framework.**

Constitutionally, municipal governments are under the jurisdiction of the provinces. This fact does not preclude federal engagement in urban issues, as is evidenced both by other countries with similar constitutional arrangements, and by the high level of federal involvement in other areas of provincial jurisdiction, such as health policy (Berdahl and Sapergia 2001). However, there are two very good reasons for including all three orders of government in an urban agenda. The first is that a tripartite model better respects Canada’s federal system – a system of great national value and importance. Indeed, any federal urban engagement model that proposes to deal bilaterally with municipal

governments would only serve to exacerbate federal-provincial and provincial-municipal tensions, to the long-term detriment of Canada's cities.

The second reason for a tripartite approach is that the actions of all three orders of government affect a city's quality of life, economy and competitiveness. Urban centres are policy sites where all three governments are inevitably and necessarily present, making policy interdependence a fact of life that can best be acknowledged through tripartite mechanisms. Failing to include all three orders of government in discussions and agreements about urban issues reduces the opportunity for governments to work together cooperatively and to address urban issues holistically. The end goals of an urban strategy are best served when all three parties are at the table. For these reasons, the federal-municipal relationship should be part of a tripartite federal-provincial-municipal relationship. In a practical sense, this means that all three orders of government act as partners in joint urban initiatives (tripartite agreements), and that the federal government formally includes both provincial and municipal governments when it consults on urban issues. (Similarly, *provincial* urban strategies are best served when both the provincial and the municipal governments are at the table.)

**Principle #3: The federal government should focus its urban engagement on Canada's large cities, with resource allocation based on fairness and regional equity.**

Canada has an estimated 4,000 incorporated municipalities, varying greatly in population size. As of the 2001 Census, 64.3% of all Canadians lived in one of 27 Census Metropolitan Areas (CMAs) – urban regions with core populations of at least 100,000. Recent debates in Canada about the importance of cities have focused almost exclusively on the needs of these big cities. The arguments about cities as economic engines and human capital centres, for example, are arguments that fit well with the big cities, but less well with smaller cities, and quite poorly with smaller municipalities. Similarly, the policy issues facing the large cities are often uniquely large city problems.

For the federal government to truly have an impact on urban issues, it is necessary that its resources and attention be focused on Canada's large cities. The Statistics Canada CMA definition of 100,000 persons should be the bare minimum for a city to qualify as a "large city." To limit the focus further, the federal government may wish to define "large city" as the dominant city or cities in a province. (The Prime Minister's Task Force focused on eight urban regions: Halifax, Montreal, Ottawa-Hull, Toronto, Winnipeg, Calgary, Edmonton and Vancouver.) The rationale for a big city focus is two-fold: first, it allows federal resources to be directed at the urban areas with the greatest impact on national and provincial quality of life and economic competitiveness, and second, it helps to prevent federal funding dollars from being spread too thinly. Simply put, the potential for positive results increases if a big cities focus is used.

However, a balance must be struck between the needs of Canada's largest cities – Toronto, Montreal and Vancouver – and the needs of the remaining large cities. Simply put, big cities engagement should not be translated into "Toronto-Montreal-Vancouver" engagement; there must be room for other large, provincially-dominant cities. An engagement model that focuses exclusively, or even primarily, on Canada's "big three" would create regional inequities in federal funding dollars, resulting in increased regional tensions among and even within provinces. It would also create a competitive advantage for select cities at the expense of the others – an important factor given that Canadian cities are competing with each other as much as with international cities for human capital, investment dollars, and businesses. A third risk with focusing on the three largest cities is that it would create the perception, if not the reality, that federal urban funding dollars are allocated primarily to areas that benefit the electoral interests of the government. (A "fund all cities, big and small" strategy would also foster this impression.) Given high levels of public cynicism towards politics in general, such a perception should be strongly avoided.

For these reasons, a federal "big cities" engagement should be based on principles of fairness. All big cities should have equitable access to federal partnerships and funding dollars. The allocation of funding resources should consider variables such as city size, region (to ensure some degree of regional equity), and the specific funding need. Regardless of the exact criteria used, a consistent and transparent set of measures should guide federal decision-making on urban engagement.

**Principle #4: Federal urban engagement should contribute to the long-term fiscal capacity of cities.**

A long-standing complaint of Canadian big city mayors is that they lack the fiscal capacity to deal with their cities' needs. As Canada West research has demonstrated, municipal governments are highly dependent on the property tax, a revenue tool that does not respond quickly to economic growth (Vander Ploeg 2001, 2002a). The result is that municipal revenues are not able to keep pace with population growth and inflation (Vander Ploeg 2001). Thus while the federal government has the capacity to grow its revenues, municipal governments must address issues of scarce resources in the face of growing demands.

One possible approach to this vertical fiscal imbalance is to develop a grant model, whereby the federal government collects revenue and then grants the funds to select cities and/or urban programs. (This is the approach pointed to in the September 2002 Federal Throne Speech.) However, there are a number of problems with this approach. One of the most detrimental problems is that grants place cities in a position of fiscal dependency. A federal (or for that matter, provincial) grant program, while it may do a tremendous amount of good while the money flows, still leaves cities with an uncertain future. There are numerous examples of city governments being orphaned by federal and provincial

governments when times get tough or when priorities change, leaving them in the difficult position of finding new revenue sources or eliminating established programs. For example, in 1992, the federal government froze its payments of grants-in-lieu of property tax – amounting to approximately \$600 million in lost municipal revenues across Canada (Federation of Canadian Municipalities 1998). How can cities be expected to plan long-term initiatives, such as an expansion of urban transit or the building of a key interchange, when grant funds are subject to such unexpected reductions? This is not to say that federal or provincial governments should eliminate grant funding as a potential approach to short-term policy issues. However, it must be clear that grant revenues do not address the issue of municipal fiscal capacity in the long-term, and leave cities overly reliant on property taxes. Another problem with grants is accountability: when revenue and expenditure decisions are made by different governments, public accountability is reduced.

If federal engagement in cities is to significantly improve life in major urban areas, it must contribute to the long-term fiscal capacity of cities. Over time, federal funding should address the vertical fiscal imbalance in Canada. This will require a significant rethinking of the allocation of resources across governments – a politically and technically difficult challenge. (Some options for beginning these discussions are raised in the final section of this paper.)

Over the short-term, it is critical that in negotiating tripartite programs, all parties keep in mind a future date when the municipal government is left alone to handle the project or program. Chances are high that, at some future date, federal and/or provincial funding priorities will change, leaving the municipal government with sole responsibility. The history of municipal finance demonstrates that transferred and joint funds are impermanent. Failing to acknowledge and plan for this strong likelihood leaves municipal governments exposed to financial uncertainty.

In practice, this means that tripartite agreements should focus on projects with clear completion dates, rather than ongoing programs. Federal funding agreements should be contingent on municipal strategies to maintain the project without federal and provincial funding after a specified date. Obviously, these parameters will limit the range of tripartite agreements possible. However, they will also prevent municipal governments from being engaged in unsustainable projects.

**Principle #5: Federal urban engagement should encourage municipal governments to focus on core municipal activities.**

Municipal governments are responsible for a variety of core activities, which typically include police and fire protection, roads, water supply, sewage and solid waste, public transit, land use planning and regulation, and other similar functions (see Sancton 1994 for a more complete list.) Although there are exceptions (such as legislated municipal delivery of social services in Ontario), in general Canadian cities are not responsible to fund income redistribution programs. One large challenge for



municipal governments, however, is that when federal and provincial governments fail to address urban social issues outside municipal responsibility (such as affordable housing and homelessness), public demands emerge for municipal governments to step into their place. These demands are coupled with a very strong municipal awareness that cities bear the social and economic brunt if these policy fields are ignored. As Vander Ploeg (2002b, 4) writes, “The presence of significant urban challenges that consistently fail to be addressed by any order of government will not contribute to the attractiveness or quality of urban life in Canada.” The political reality, therefore, is that municipal governments are left with extensive de facto residual responsibilities and often engage themselves in policy areas that are outside their existing core competencies and beyond their fiscal resources. While this municipal engagement in non-core fields is legally an option in many provinces (Wong 2002), it is not a sustainable position for cities as they are currently financed.

Some analysts would argue that the current allocation of municipal core responsibilities is inappropriate, and that the provincial governments should be formally transferring a number of social policy responsibilities – along with the revenues to address these new responsibilities – to municipalities. This may be true, although it is worth noting that there is limited public interest in expanding municipal powers (Berdahl 2001). However, regardless of the validity of arguments about appropriate municipal responsibilities, the fact remains that municipal responsibilities, core or otherwise, must be determined by the *provincial* government, ideally in negotiation with the municipal governments (such as is being done in Alberta through the Minister's Council on Roles, Responsibilities and Resources). There is no federal role in this assignment of responsibilities.

For this reason, the federal engagement in urban issues should be structured in a way that encourages municipalities to focus on municipal core competencies as they now stand, and ensures that federal engagement is not used (either intentionally or inadvertently) to broaden municipal responsibilities. As the first step toward this end, the federal government should be aware of the urban impact of federal policy, and be highly sensitive to the fact that if the federal government fails to fully address policy issues within its domain, the result may be increased pressure on municipal governments. Two examples can be noted here. First, federal disengagement from affordable housing policy is argued to have had tremendous impact on Canada's cities (Orr 2000). Second, disagreements between federal and provincial governments over jurisdictional responsibility for urban Aboriginal people have resulted in a policy vacuum: “In the absence of federal or provincial action, municipalities have often been left to create policies to provide for the needs of urban Aboriginal people – and frequently lacked capacity to do so adequately” (Hanselmann 2001, 10). In short, the federal government should avoid off-loading its policy responsibilities, and should actively evaluate the impact of federal policies on cities. These evaluations should include formal consultation with municipal and provincial governments, as discussed later in this paper.

Second, to avoid pulling municipal governments into fields outside their core responsibilities, the federal government should limit its tripartite agreements to policy areas clearly among municipal responsibilities. In other words, a tripartite infrastructure program or urban transit agreement is preferable to a tripartite homeless shelter initiative. (This is not to say that the federal government should not fund a homeless shelter, but rather that *municipal* governments should not be made jointly responsible to fund social issues such as homelessness unless they have been legislated responsibility and resources to do so.) Given their financial pressures, along with a strong desire to ensure the long-term wellbeing of their cities, it is difficult for municipal governments to resist the temptation of federal revenue – even if the revenue agreement pulls them outside their core competencies. The federal government should avoid placing municipal governments in this difficult and unsustainable position.

It must be recognized that a complete disentanglement of municipalities from issues outside their core responsibilities may not be possible. The reality is that municipal governments already have complex entanglements. What is possible, however, is to structure federal urban engagement on the principle of encouraging municipalities to focus on core municipal responsibilities. Doing so better respects jurisdictional responsibility, and prevents further strains on long-term municipal fiscal capacity.

**Principle #6: Federal urban engagement should bring municipalities in as partners, but should not require equal funding of tripartite agreements.**

There have been a number of examples of federal-provincial-municipal agreements in Canada, including infrastructure projects and urban economic development agreements. The form of these tripartite agreements has varied over time and across provinces. Frequently, municipal governments are an equal funding partner, responsible for providing one third of the funding, with the federal and provincial governments each also providing one third. In other agreements, municipal governments have been allowed to participate at a lower funding level. In some agreements, municipal governments are given an equal decision-making role, while in others municipal governments have limited decision-making authority.

This variability has provided some important lessons. The first is that municipal governments express strong concerns (and rightly so) when they are not allowed to fully participate at the decision-making table. This lack of authority undermines the municipality's ability to represent the interests of its citizens and reduces local control over projects. It also creates significant differences in municipal voice across the country, as some provinces allow their municipal governments to sit at the table while others do not.

The second lesson is that municipal governments, with significantly fewer fiscal resources than federal or provincial governments, experience considerable financial strain if required to provide a full third of the project's funds. This strain can distort local funding priorities, negatively affect long-term municipal fiscal capacity, and even limit local ability to participate in joint projects. As Wong (2002, 13) writes, "... although tripartite agreements such as the [Infrastructure Canada Program] are beneficial to cities, equal cost sharing among the federal, provincial and municipal governments [strains] the limited city finances. Some [municipal officials] doubt that cities could handle two IPC-like agreements at any one time." If municipal governments cannot carry the financial load necessary to participate in a program, the program is useless to them.

To address these factors, the federal government should require that tripartite agreements allow municipal governments to sit as equal decision-making partners, and should allow for flexibility in the funding requirements for cities. In addition, to ensure public awareness of government cooperation, all participating governments should receive appropriate public acknowledgement of their role.

**Principle #7: Federal urban engagement should place an emphasis on federal, provincial and municipal policy innovation.**

Given the magnitude of urban challenges facing Canada in the years ahead, it is clear that innovative thinking is required. If Canadian governments (be they federal, provincial or municipal) fail to identify new solutions to municipal problems, the result will likely be a failure to resolve those problems. Policy innovation is needed among all participating governments. This necessarily implies a re-examination of existing approaches and assumptions, and learning from cities in other countries to see what lessons, if any, can be transferred to the Canadian context.

How can the federal government improve Canadian cities through policy innovation? The first step is for the federal government to "get its own house in order," and re-examine through an urban lens the incentives and disincentives in existing programs. As the work of the National Round Table on the Economy and the Environment (Salsberg 2002) demonstrates, there are a number of federal policies that work against long-term urban interests. Examples include a GST rebate for new housing but not for the renovation of existing housing stock, and tax incentives for individuals to drive to work and disincentives for individuals to take public transit – a tax system that encourages urban sprawl, and by extension the expansion of costly urban infrastructure (Salsberg 2002).

The federal government can also encourage innovation in tripartite funding agreements. It is often said that federalism allows for a "policy laboratory": individual provinces have the flexibility to use new approaches to policy problems, and the opportunity to learn from the successes and failures of their neighbours. A similar argument can be made about Canada's cities: there is tremendous opportunity

for cities to experiment locally, and to share the lessons with other municipalities. An incentive structure could be created if proposed tripartite projects were evaluated on their use of innovative local approaches in addition to other factors. To ensure transferable lessons, projects could require clear evaluation measures at the start.

Lastly, the federal government could also participate in national discussions, with provincial and municipal governments about urban policy innovation. The purpose of these discussions would not be to establish tripartite agreements – although that may be an outcome in some circumstances – but rather to encourage all governments to be creative and flexible in their solutions to urban challenges.

### Principles of Federal Engagement in Cities: Summary

<b>Principle #1: Local determination of local policy priorities</b>	
Rationale	Municipal governments are in the best position to identify key urban policy priorities.
Risks if not followed	Distortion of municipal funding priorities; lack of innovation; erosion of local control.
Practical Implications	Municipal governments should be given some formal mechanism for communicating local priorities to the federal government. Local priorities should be the focus of tripartite agreements.
<b>Principle #2: Tripartite framework</b>	
Rationale	Respect for federalism.
Risks if not followed	Deteriorating federal-provincial and provincial-municipal intergovernmental relations; lack of a holistic approach to urban policy issues.
Practical Implications	The federal government should ensure that both provincial and municipal governments are partners in its urban agreements, and develop formal mechanisms to consult with provincial and municipal governments on urban issues.
<b>Principle #3: Big cities focus, based on fairness and regional equity</b>	
Rationale	Allows federal resources to be directed at the urban areas with the greatest impact on national and provincial quality of life and economic competitiveness; helps to prevent federal funding dollars from being spread too thinly.
Risks if not followed	Regional inequities in federal funding dollars, resulting in increased regional tensions; a competitive advantage for select Canadian cities; political pressures for federal government to fund projects in strategic political locations over cities in need.
Practical Implications	A consistent and transparent set of measures should guide federal decision-making on urban engagement. Variables to be considered might include city size, region, and the specific funding need.
<b>Principle #4: Contribute to long-term municipal fiscal capacity</b>	
Rationale	Ensures long-term, stable funding; reduces municipal reliance on property tax and grants.
Risks if not followed	Continuation of a funding model that has demonstrated itself to be insufficient in meeting municipal finance needs; increased problems with accountability.
Practical Implications	Federal, provincial and municipal governments should begin discussions of policy options for the federal government to contribute to municipal funding. Over the long-term, federal funding should address the vertical fiscal imbalance in Canada.

**Principles of Federal Engagement in Cities: Summary (continued)**

<b>Principle #5: Focus on municipal core activities</b>	
Rationale	Respect for jurisdictional responsibility; ensures long-term municipal fiscal capacity.
Risks if not followed	Municipal governments could be pulled into policy areas outside their responsibilities, thereby inflating public expectations and creating long-term fiscal strain.
Practical Implications	The federal government should ensure that it is not off-loading its responsibilities to municipal governments. Tripartite agreements should focus on key municipal roles rather than on issues outside municipal responsibility.
<b>Principle #6: Municipalities as partners, but not necessarily equal funders of tripartite agreements</b>	
Rationale	Ensures local voice; reduces vertical fiscal imbalance; promotes long-term municipal fiscal capacity.
Risks if not followed	Inability of municipalities to participate; distortion of municipal funding priorities; lack of innovation and local control; long-term municipal fiscal strain; inconsistency across provinces.
Practical Implications	In tripartite agreements, federal, provincial and municipal governments should each have a voice at the table. Municipal governments should not be required to provide one-third of the funding in order to participate. On joint agreements, all governments should receive appropriate public acknowledgement.
<b>Principle #7: Emphasis on innovation.</b>	
Rationale	Federalism as “policy laboratory”; encourages new approaches and learning.
Risks if not followed	Failure to identify new solutions to municipal problems, which may result in a failure to resolve urban problems.
Practical Implications	The federal government should re-examine through an urban lens the incentives and disincentives in existing federal programs. Tripartite agreement funding decisions should reward municipalities that propose innovative local approaches, coupled with clear evaluation measures.

*Increasing Federal Awareness of Its Urban Impact*

A common complaint from municipal governments is that the federal government does not adequately consider the impact of its policies on urban areas, despite the fact that many federal policies have significant urban dimensions and ramifications. (A similar complaint is often levels at provincial governments.) There is a tendency to consider “urban issues” as solely those issues addressed by municipal governments. However, “[w]hile many concerns can be tagged as ‘urban issues’ it does not logically follow that local governments are responsible for them...” (Vander Ploeg 2002b, 3). This point was acknowledged by the Prime Minister’s Caucus Task Force on Urban Issues, which writes, “The Government of Canada has always shown an interest and played a key role in urban life. .... [It] is a significant investor in urban areas, both in terms of its physical presence and the services it delivers. .... Many federal departments have a stake in urban issues through national objectives and international obligations” (2002, 8).

The question, then, is how can the federal government ensure that its own policy actions – be they explicitly urban policies or not – work for the betterment of Canada’s cities? Stated another way, what steps could the federal government take to improve its awareness of the impact of federal policies on cities? There are at least three options: the creation of formal consultation mechanisms; the ministerial assignment of urban issues; and the adoption of a federal “urban lens.” It is possible for the federal government to adopt all three of these strategies in a complementary manner.

**Formal, regular tripartite consultation.** A key problem with the current federal-provincial-municipal intergovernmental structure is that there are no formal mechanisms for regular consultation among all parties. Communications tend to be ad hoc, and this ad hocery limits the ability of Canadian governments to work together to address urban issues (Wong 2002). One solution to this would be the establishment of a federal Standing Committee on Urban Affairs, with the committee responsible to conduct regular consultations with provincial municipal affairs officials and municipal governments. The Standing Committee would be required to examine issues across a variety of policy fields, including (but not limited to) finance, infrastructure, and the environment. The committee would consult with provincial and municipal representatives on a regularly scheduled basis, allowing for a consistent urban perspective in national policymaking. The purpose of the consultations would not be to give provincial and municipal governments a role in federal decision-making, but rather to ensure that the perspectives of big cities are taken into account in federal decision-making. The regular consultations would also create stronger tripartite relationships, and would address the Task Force’s desire for “all orders of government to coordinate resources, and consult and collaborate on a new approach to the challenges in Canada’s urban regions” (2002, vi).

One challenge, however, is that while it is easy to figure out who participates on the federal and provincial sides, determining municipal participation is not as easy. Assuming a federal “big cities” strategy, with a focus on a small number of Canada’s largest and provincially-dominant cities, municipal participation should be limited to those cities, with each city representing its own interests. This focus would help the federal government avoid the pressures to include all Canadian cities, which would result in an unworkable committee structure and a “watering down” of large urban concerns.

**Ministerial assignment of urban issues.** While tripartite consultation would improve vertical policy integration, there is still a need to coordinate policies horizontally – that is to say, there needs to be coordination among federal departments, as well as between federal, provincial and municipal governments. Without a single ministry responsible to coordinate the various federal urban policies, department-specific urban initiatives “might lead to overlapping programs and conflicting criteria for eligibility” (Wong 2002, 10). A single ministry responsible for urban affairs (be it a newly created

ministry or the assignment of urban affairs to an existing ministry) would increase the national profile of urban issues and encourage a holistic federal approach to cities. To be fully effective, this ministerial approach should be combined with formal, regular consultations (perhaps conducted by the Standing Committee); on its own, a ministerial approach does not allow for municipal and provincial identification of local priorities or perspectives.

**Federal Urban Lens.** One option for increasing federal awareness of urban issues is the adoption of an “urban lens” to evaluate existing and future federal policy. The Prime Minister’s Caucus Task Force asserts, “We need to apply an urban ‘lens’ to all policies and programs, both national and international that are directed at urban regions. An urban perspective will guide future legislation and policies so that programs designed for urban centres can be assessed for both negative and positive consequences” (2002, 3). Presumably, an urban lens would operate similarly to the existing federal rural lens, which requires federal policymakers to answer a number of questions prior to implementing a new policy. Examples of these questions include: “How is this initiative relevant to rural and remote Canada? Have the most likely positive and negative effects on rural Canadians been identified and, where relevant, addressed? Have rural Canadians been consulted during the development or modification of the initiative?” (Rural Secretariat 2002). Addressing similar questions for urban policy would be beneficial; ideally, municipal and provincial governments would be consulted in answering these questions.

The very need for an urban lens raises an intriguing question. Why is it, in a country where six in ten live in large urban areas, the federal government must be reminded to think about urban issues? Why is it that the federal government had a “rural lens” and rural secretariat long before entertaining questions about urban Canada? (Ironically, the Task Force notes that the federal government’s successful approach to rural Canada should serve as its model for focusing on urban issues.) These are questions that the federal government may wish to consider as it moves ahead.

### *Funding Canada’s Cities: A Tripartite Approach*

One of the largest challenges facing Canada’s big cities is urban finance: municipal governments regularly report high expenditure demands (particularly for maintaining and building urban infrastructure), insufficient revenues, a lack of diversity in tax sources, and unreliable transfer revenue from federal and provincial governments. For this reason, one of the principles underlying federal urban engagement should be to contribute to the long-term fiscal capacity of cities (principle #4), ideally by improving the allocation of tax revenues rather than by increasing total taxation levels. But how can federal, provincial and municipal governments work together cooperatively to address this urban finance challenge? What are some examples of policy tools that might be employed?

To contain municipal expenditures, the most important role the federal government can play is to make certain that its urban engagement enables municipal governments to focus on their core responsibilities by ensuring that federal responsibilities are not off-loaded to cities and by focusing partnerships on municipal core areas (principle #5). Other expenditure issues reflect the balance of roles and responsibilities between provincial and municipal governments, and must be negotiated bilaterally. It is worth noting that numerous governments and municipal associations in Canada have been working to clarify municipal roles and responsibilities, with the potential goal of reducing or eliminating municipal participation in non-core areas. For example, Alberta Municipal Affairs established the Minister's Council on Roles, Responsibilities and Resources in 2001. There are also cases in western Canada of municipal governments uploading service responsibilities to provincial governments (Vander Ploeg 2002). The point to stress is that the re-alignment of municipal responsibilities is *not* an area suited to a tripartite approach.

There is a much greater range of options for tripartite approaches to addressing municipal revenues.

**Tripartite Agreements.** As noted earlier in this paper, one option is the use of tripartite agreements as a short-term tool to address strategic core municipal issues, which appears to be the direction in which the federal government is currently headed. Tripartite agreements have been used on a number of occasions in Canada, with mixed reviews. There are “a number of shortfalls in current tripartite agreements – chiefly their short life, sporadic nature, financial burden on cities, and inconsistent participation of municipalities – that leave city authorities unable to take full advantage of these agreements” (Wong 2002, 13). To address some of these concerns, the federal government should ensure that tripartite agreements reflect local priorities (principle #1), allow for flexibility in municipal contribution levels (principle #6), and anticipate municipal sole financial responsibility at the completion of the agreements. At the same time, all governments must recognize that tripartite agreements do not represent a long-term solution to Canada’s urban finance problems. At the end of any given tripartite agreement, a municipal government may have completed a specific project, but it is left to deal with the issues of insufficient and inconsistent revenues. Thus, it is critical that governments work cooperatively to address the vertical fiscal imbalance in Canada through the creation of new, reliable revenue tools for municipal governments.

**Federal-Municipal Tax-Sharing.** A longer-term option to address municipal finance is tax-sharing, which is used in a number of federal countries. In the United States, shared taxes are limited to state (not federal) sources and include sales, fuel, liquor, gambling and other taxes (Vander Ploeg 2002a). These shared tax revenues are typically earmarked for specific expenditure purposes. In Germany, “apart from the taxes they levy, municipalities are also entitled to a specific share of the revenue raised



by federal and state governments from income and general sales tax,” and the majority of municipal revenue comes from federal and state transfers (Steytler 2002, 16). In Australia, there is no formal tax-sharing, but the federal government does provide regular, per capita unconditional grants to the states, to be reallocated to municipal governments for general purposes – in effect, a federal equalization payment to local governments (Berdahl and Sapergia 2001).

Tax-sharing in Canada is highly limited, and is strictly a provincial-municipal issue. However, there is a growing demand for federal-municipal tax-sharing. As Calgary Mayor Dave Bronconnier (2002) writes, “Cities don’t want more handouts subject to the whims of the federal government. They want a fair and stable share of the tax revenue they generate to fund critical infrastructure projects. .... It is time for the federal government and the provinces to stop looking at municipalities as competitors for tax dollars and recognize that an equitable reallocation of the tax revenue currently collected, rather than handouts, will keep our cities growing and our country strong.” An idea that is often raised in urban finance discussions is reallocation of the federal fuel tax (in whole or in part) to large cities. (It should be noted that there is competition for the federal fuel tax: the transportation sector often argues that the tax should be dedicated to infrastructure spending.) To respect the principles of federalism, transferred funds – be they from the fuel tax or any other tax source – would need to be directed to the provinces for redistribution to the large cities (similar to the Australian model).

If this is to occur, there are two issues that must be addressed. First, some conditions must be put on the transferred revenues to ensure that the provinces allocate the revenues to the targeted municipalities without conditions. Here, a lesson can be drawn from the Australian experience, where an equalization formula guides the grant distribution (Steytler 2002). Second, the transfer of revenues must be constructed in a way that protects municipalities from arbitrary federal budget cuts. An illustration of this risk was seen in one of Canada’s few tax-sharing agreements. The Alberta government has an agreement with the Cities of Calgary and Edmonton to share with them five cents per litre of fuel sold in each city (point of sale tax-sharing). In early 2002, the Alberta government announced plans to unilaterally reduce Edmonton and Calgary’s share of gasoline tax revenues. While this decision was ultimately reversed (due to strong lobbying by the two mayors), the fact that it was raised at all points to the instability of tax-sharing. (Provincial governments experienced a similar problem in the 1990s, when the federal government unilaterally and unexpectedly cut its transfer payments to provinces in an effort to eliminate the federal deficit.) Part of the problem appears to have been the fact that the tax-sharing was structured similar to a grant in provincial budgetary terms. One possible approach to increase the stability and longevity of tax-sharing would be to state the tax-sharing formula in legislation (thus making unilateral changes more difficult), and having tax-shared amounts accounted for in budgetary revenue items, rather than treated as expenditure items.

One challenge with federal-municipal tax-sharing is that the end result is reduced federal tax revenue available for funding other policy areas—assuming, of course, no increase in taxation. This reduces the appeal of this option for the federal government.

**Municipal Bonds.** Another tripartite option to address municipal finance over the longer-term is the use of tax-free municipal (or community) bonds for debt financing of infrastructure projects. Indeed, this is an idea being pursued in Ontario; the May 2002 Speech from the Throne promised legislation to allow municipalities to offer “Opportunity Bonds tax-free to investors, allowing for more infrastructure development and giving municipalities more control at the local level” (Government of Ontario 2002). The federal and provincial governments could play an important role in municipal bonds if each were to exempt all or a portion of the interest paid to the bond owner from taxes and/or provide a tax break to holders of municipal bonds. In essence, then, the federal and provincial governments each forego tax revenue for the purposes of increasing the incentives for investors to fund local projects.

Vander Ploeg (2002a, 14) writes, “The advantage to the city of community bonds is borrowing at a lower rate of interest. The advantage to citizens is an opportunity to participate in the building process through a relatively stable and tax-free investment.” Municipal bonds are widely used in the United States, and it is reported “the U.S. municipal bond market is viewed around the world as a model of liquidity, efficiency, and security” (Chamberlin and Weinstein 2002). Although their usage in Canada would require changes to provincial legislation, the federal government could facilitate discussions on how the three orders of government can work together to develop municipal bonds. This discussion would need to include careful assessment of the advantages and disadvantages of municipal bonds as a debt-financing tool.

**Creating Tax Room for Expanded Municipal Tax Tools.** Yet another option – and one frequently voiced in municipal finance debates – is allowing municipal governments access to a greater number of own-source tax tools, such as a municipal income or sales tax. Ultimately, this is a point for provincial-municipal negotiation (see Vander Ploeg 2002a, 2002b for one possible approach). However, the federal government can play a significant role in this regard. One key concern about allowing large cities greater taxing authority is that the result could be higher overall taxation levels in Canada – and as we often hear, “there is only one taxpayer.” The question that must be raised, then, is how can tax dollars be most effectively allocated among all three orders of government? The immediate response to this question has been a grants approach, as noted earlier. There are a number of problems with grant revenue, including instability of revenues, a reduction in accountability, the inability of municipal governments to set the revenue rates, and the costs of administration involved in transferring funds from one government to another. If the federal government is to truly contribute

to the long-term fiscal capacity of cities, it will at some point need to examine issues of vertical fiscal inequality. This may mean a reduction in federal taxation, for the purposes of allowing municipal governments greater tax room within which to employ new tax tools.

How could the federal government ensure that its tax reduction would be used for municipal tax room? One approach might be to transfer income tax points to provinces, contingent on that income tax room being used for big cities. (A model here is the transfer of federal income tax points to the provinces for the purpose of health care funding.) The considerable political hurdle is one of “political credit”: once the transfer has occurred, the federal government might no longer get acknowledgement for its support for cities. Another hurdle, of course, is reduced federal tax revenue available for funding other policy areas. The mechanics of how federal tax room might be freed up for municipal purposes would require considerable research and debate. The main point is that it will be difficult for provincial governments to provide new tax tools to cities if this action is publicly perceived to create higher levels of taxation. The federal government can create an opportunity for provinces to allow new municipal tax tools by lowering its own tax take.

Overall, there is a range of options – from tripartite short-term project funding to tax-sharing to municipal bonds to a rethinking of taxation in Canada – that all governments can consider in the quest to develop urban revenue tools. Indeed, a myriad of other tripartite options to address municipal finance are likely to surface in the years ahead. The point to stress is that Canada needs to begin tripartite discussions about the creation of new, stable fiscal tools for cities – ideally, tools that allow municipal governments to set (and be accountable for) their own revenue rates. The federal government, working cooperatively with provincial and municipal governments, can play an important role in this regard.

### *Conclusion*

There is considerable political momentum behind the cities issue. Urban issues are clearly on national and provincial political agendas, and are beginning to attract the attention of Canada’s corporate sector. It is this position on the political agenda that simultaneously represents the greatest opportunity and the greatest threat for Canada’s large cities. The opportunity lies in the political will and interest, which creates the potential to address not only immediate policy concerns but also structural issues facing cities, such as the vertical fiscal imbalance and the need for greater federal and provincial awareness of urban challenges. The challenge facing Canadians is to take this window of opportunity, this position on the national political agenda, and use it wisely. There is reason to be concerned that, due to impatience, short-term thinking, or a lack of creativity, Canada will fail to

address the structural issues, or worse, that hasty or politically expedient decisions will create new urban problems.

It is for this reason that federal urban engagement must be grounded in key principles that work to the long-term benefit of Canada's large cities. Are Canadians and their governments prepared to do the hard work necessary to ensure viable cities for generations to come? It is this question that must be answered – through actions, not words – in the months and years to come. ■

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