Toward more efficient municipal government in Canada

Part 1: Municipalities a growing force

Guest Commentary

by Bruce Hollands

Municipalities – a growing force, a growing concern

In Canada, the power of municipalities continues to grow, something that could have serious effects on taxpayers if left unchecked.

Several landmark court decisions – some that include the Supreme Court of Canada – have granted municipalities greater discretionary authority and operating freedom. Memoranda of Understanding signed by the Union of British Columbia Municipalities and the Association of Municipalities of Ontario with their respective provincial governments have entrenched the principle of consultation in areas of provincial prerogative.

As well, billions of dollars have been transferred from the federal, provincial and territorial governments to municipalities for infrastructure renewal — exceeding $20 billion since the 1990s. Most taxpayers are unaware of this financial assistance, and rarely are these revenues mentioned in discussions about fiscally strapped municipalities. Instead, we are reminded by organizations like the Federation of Canadian Municipalities (FCM) and the 18 provincial and territorial municipal associations that local governments collect only 8 cents on every tax dollar, and that the provinces and federal government receive the lion's share: 42 cents and 50 cents from every dollar, respectively.

The notion that municipalities need greater revenues from senior levels of government may appear to have merit. However, municipal spending has not been adequately scrutinized to fully support the concept. Are purchasing processes as competitive as they can be? Could Canadian municipalities operate more efficiently? Have alternative delivery mechanisms been fully exploited? Are municipalities doing too many things, allowing core services to suffer?

This piece, the first in a special three-part series on efficiency in municipal government, tells the real story of growth in local government revenues and argues in favour of more competitive purchasing and public-private partnerships. Provincial downloading will not be addressed, since by and large, local governments have been receiving the revenues needed to meet their provincial obligations.

> “Water and wastewater operations, accounting for between 20 and 50 percent of total municipal expenditures”

More revenues, more demands, more taxes

The revenue picture for local governments has been steadily improving, and has indeed never been better. In addition to the more than $20 billion received in infrastructure program funding noted above, in 2004 the municipal GST rebate (a return of GST paid by munici-

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palities from their purchase of products and services) increased from 57.14 percent – representing $775 million per fiscal year – to 100 percent, resulting in an extra $580 million annually for municipalities. Still more revenue has come by way of a share of the federal gas tax under the New Deal for Cities and Communities, worth $600 million in 2005-2006 and slated to reach $2 billion annually in 2009-2010. Provincial governments are also contributing significantly to the municipal bottom line through various annual grants and by sharing a portion of their own gas tax revenues.

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Yet demands for additional tax revenues continue, and municipalities are getting the authority to raise them. Toronto's new taxation powers granted under Ontario's *City of Toronto Act*, gives the city broad and permissive powers limited only by exclusions, making the list of potential new taxes almost limitless.

Toronto Comes of Age – At Your Expense

Toronto Councillor Shelly Carroll's comment that Toronto "came of age" on October 22, 2007, after city council voted for new taxes on land transfers and personal vehicles is prophetic. Other municipalities in Ontario and across Canada are already clamouring for similar new taxation powers. What does the future hold?

A recent FCM press release suggests that we can expect more of the same: "… until municipalities receive the equivalent of one cent of the GST, property taxes will continue to increase…" (October 11, 2007). The previous

FCM demand was for a share of the federal gas tax; now it's for a portion of the GST.

Competition, Competition, Competition

When it comes to purchasing, municipalities can behave like sovereign countries, arbitrarily excluding innovative and efficient products and services, with no recourse for the private sector except through lengthy and costly lobbying efforts. Taxpayers get handed the bill.

For example, a product certified by all required international, national and provincial agencies, and used by other municipalities in Canada, can be excluded from a tender if municipal staff so choose. This means less competition, resulting in higher prices for goods purchased by local governments. And higher front-end costs are only part of the story – tendering that is less competitive has costly cas-

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cading effects further down the line.

Water and wastewater operations, accounting for between 20 and 50 percent of total municipal expenditures, are a case in point. Modern pipe materials, like polyvinyl chloride (PVC) are corrosion proof, giving them superior longevity. As well, their ultra smooth surfaces mean that less energy is needed to pump water through them (which represents as much as seven percent of Canada's electricity consumption and accounts for 70 to 90 percent of a municipal water utility's operating costs). PVC is also less prone to leaks, which average between 20 and 50 percent in most water distribution systems. However, these pipes continue to be excluded from select municipal tenders, even if it would make economic sense to use them, given their lower operating and life-cycle costs.

Collectively, municipalities spend about $50 billion annually, accounting for about 11 percent of total government spending in Canada. According to most experts, more competitive purchasing procedures could easily yield $2 - $5 billion in savings across the municipal sector. And this is at the purchasing end of the spectrum. Operational savings could also be in the billions.

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More Public-Private Partnerships (P3's)

Although P3's have multiple advantages, they remain underutilized in the municipal sector. British Columbia has made some inroads in this area by requiring municipalities receiving provincial funding to tender all infrastructure projects above $20 million as P3's. This has helped leverage a great number of projects; however, since they are all designated as design, build, finance and operate (DBFO), only large consortia can compete. If project thresholds were lowered to $1 million and proposal criteria limited to design and build (DB), more local companies could get involved, spurring even more competition and innovation.

An excellent example of how P3's can leverage public funds is a $25-million, 5,500-seat arena in Chilliwack, built using only $6 million in public funds, with the private sector investing the rest. Abbotsford's 7,000-seat arena, on the other hand, is totally funded from public monies and will cost taxpayers more than $55 million. And the project is already over budget, because risks have not been properly transferred to the private sector, which would have been the case had a P3 been used. Not surprisingly, Abbotsford's council just voted for a 16

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percent tax increase.

A recent poll conducted by the Canadian Council for Public-Private Partnerships, Environics and Research Group shows that 64 percent of Canadians agree that “It’s time to allow the private sector to deliver these types of services in partnerships with governments.” Yet unions and municipalities remain largely opposed. This position is not in line with voter interests. Perhaps it is all about self-interest.

Infrastructure Crises

The Canadian Water and Wastewater Association estimates that $60 - $100 billion will be needed just to refurbish existing water and wastewater infrastructure in Canada. Without P3’s, competitive tendering and municipalities operating more efficiently, Canadian taxpayers will be stuck footing the bill. Using additional tax dollars to prop up inefficient local governments will only worsen the impending infrastructure crises, because the impetus for change is seldom encouraged when a service is managed by the non-competitive public sector.

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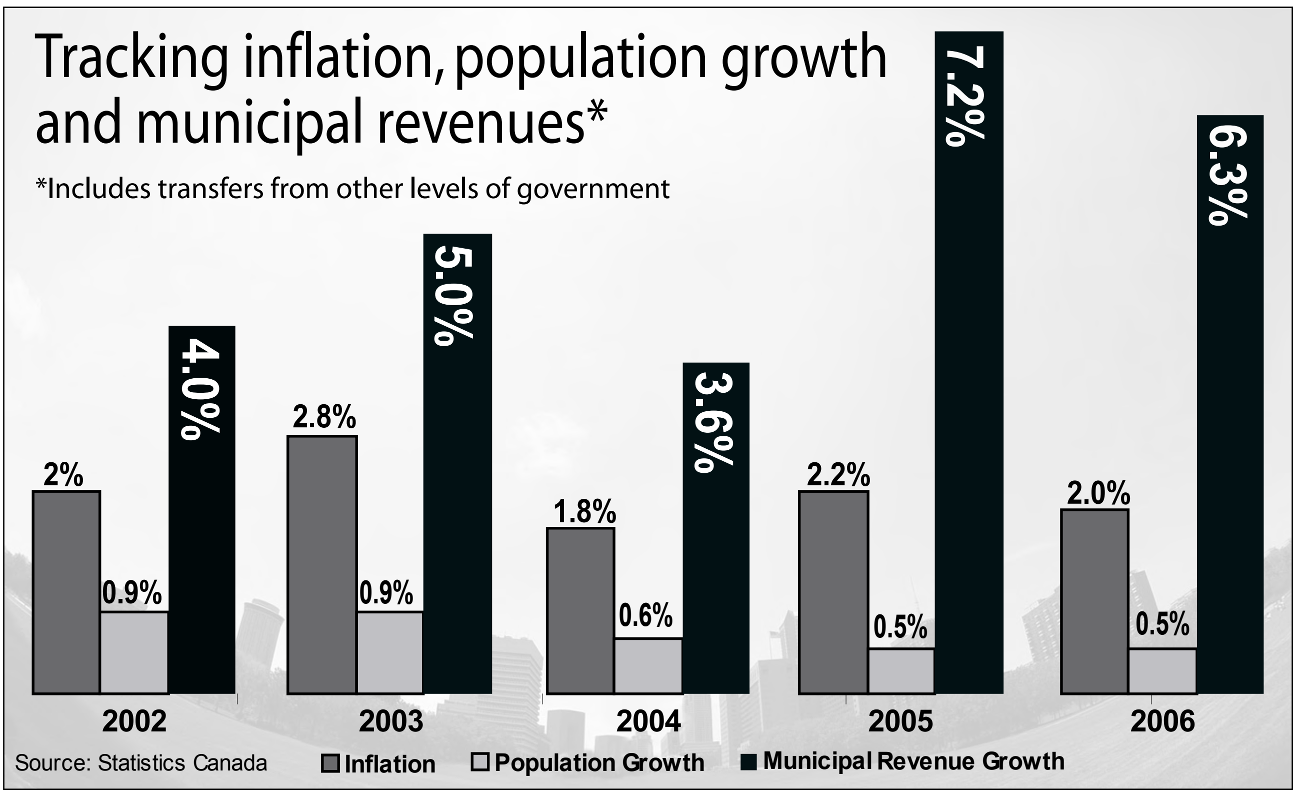

Canadian Taxpayers Federation

Part 2: New Approaches

Guest commentary
by Bruce Hollands

New Approaches

In part one of our three-part series, we argued that, left unchecked, the growing power of municipal governments could have deleterious effects on taxpayers' pocketbooks. Contrary to the claims of municipalities that they are cash-strapped, their revenues have steadily increased over the last two decades, keeping ahead of inflation and population growth.

The answer to the "woes" of municipalities does not lie with higher property taxes, new municipal taxation powers or a blank cheque from other levels of governments. It lies rather with more competitive tendering, increased operational efficiencies and greater use of public-private partnerships (P3s). Such practices could keep costs under control, while delivering greater value for tax dollars.

For example, through P3s local governments could significantly increase the number of infrastructure projects funded by the federal government's $33 billion Building Canada Plan. Underscoring the benefits of P3s at a recent conference, federal Finance Minister Jim Flaherty said: "When contributions by other levels of government and the private sector are taken into account … we should be able to leverage more than $100 billion in investment in infrastructure over the course of the next seven years in Canada." This would go a long way in helping alleviate the impending infrastructure crisis we hear so much about.

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Political Will

Keeping property tax increases in check will require setting priorities, better management and new approaches to service delivery. However, without political will, the municipal juggernaut will never be brought under control. Nowhere is that will more important than in standing up to civic unions.

The New Rich — Unionized Public Employees

When considering their salaries, benefits and pensions, it would not be far off the mark to say unionized municipal employees are Canada's new rich. For example, the average salary for the City of Ottawa's 16,000 employees is $80,000 per year, much higher than the Canadian average, which is $50,000,

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less the generous pension. To receive a pension similar to that of a municipal employee, the average Canadian would have to save millions of dollars in RSPs. All told, employee salaries and benefits now absorb 50 percent of most municipal budgets.

The only way for municipalities to lower labour costs is to outsource more services and reduce the number of union employees. This will be difficult because the Canadian Union of Public Employees (CUPE), which represents municipal workers across Canada, is a powerful organization that can deploy resources into any municipality. At the time of writing, CUPE is threatening Hamilton with a strike because of the city's demand to double the percentage of casual workers from 10 to 20 per cent. This proposal would help Hamilton reduce a projected 6 to 7 per cent tax increase for 2008.

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Examples of how unions distort and undermine municipal budgets include unreasonable overtime benefits and policies like "first-right of refusal (FRR)" – which grants privileges to workers with the most seniority. In some cases, FRR guidelines ensure that seniority determines who is first offered overtime hours. In municipalities this combination, along with poor management, has allowed some bus drivers to earn as much as $100,000 per year.

More Outsourcing and User Fees

The Economic Opportunities Commission report from Winnipeg — highlighted in the last issue of *The Taxpayer* — provides good examples of how municipalities can improve their bottom lines through outsourcing and

the increased use of cost-recovery fees. Tremendous savings could be achieved if municipalities outsourced basic services like issuing permits, information management, street and traffic light maintenance, public works equipment and maintenance, snow plowing and facilities management, to name a few.

And, by outsourcing facilities management, savings in the order of 10% could be achieved. Several public sector organizations have already done so: including, among others, Public Works and Governments Services Canada, Ontario Realty Corporation, British Columbia Buildings Corporation and Canada Post Corporation. For a municipality the size

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of Ottawa or Edmonton, this would represent about $10 to $13 million in annual savings, or the equivalent of a one percent tax reduction.

Studies have shown that contracting out has resulted in few, if any, layoffs of public employees and that they receive comparable wages and benefits from private sector employers. Labour costs are reduced over time through attrition, something governments have shown they are not very good at. Where facilities management is outsourced, the municipality would retain control over all assets and continue to exercise all responsibilities inherent to that role. To ensure that the contractor offers the best possible salary and benefits package for affected employees, the Request for Proposal (RFP) should contain a heavily weighted section for salaries and benefits, as well as opportunities for enhanced employee mobility.

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Outsourcing has a multiplier effect on the economy as well because it helps strengthen private companies or start new ones, which can then invest locally and create more jobs. In this way, municipal governments could be true enablers of local economic development.

Greater efficiencies and revenues could also be realized through increased use of user fees. These minimize the use of some services, thereby reducing consumption and the need for costly infrastructure investments. Even the Institute for Research on Public Policy, which favours greater taxation powers for cities, agrees that municipalities should “increase the use of frequently overlooked revenue sources that are within [their] control, such as user fees, and exploit the cash generating potential of municipal services like water, sewage, garbage disposal and transit.”

Managing the “Infrastructure Deficit”

It has become common currency for local politicians to argue that their federal and provincial counterparts are robbing Peter to pay Paul. To wit: income and consumption tax breaks, they say, are essentially municipal

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revenues that have been wrongly used to convince citizens they are getting tax relief. This absolves them of any responsibility for increasing property taxes.

All three levels of government will have to work together to deal with the looming infrastructure deficit, which the Federation of Canadian Municipalities (FCM) estimates to be $123 billion. Contrary to what many local officials claim, municipal revenue shortfalls are not linked to this deficit nor do we know its full extent. For instance, the latest FCM study on the infrastructure deficit admits that the report "does not provide an exhaustive or complete account of the physical condition of municipal infrastructure." And this study is the basis for the municipal sector's latest demand for a share of the GST. In fact, only 85 of the 166 municipalities surveyed responded in full or partially, representing only 46 per cent of Canada's population.

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With all the clamour about the infrastructure deficit since the 1980s, the response rate to FCM's survey should have been much higher. More importantly, was such a survey needed? Shouldn't municipal authorities know the state of infrastructure within their jurisdictions? Their failure in this regard is proof positive that they are inadequately managing their assets and cannot be trusted with federal and provincial revenues without stringent spending guidelines.

Municipalities Must Get Their Houses in Order

Experience in many municipalities over the last three decades confirms that municipal governments could collectively save billions through better management and improved service delivery. Clearly, the union genie must be put back in its bottle. More services need to be outsourced to the private sector and greater use of user fees must be considered. However, little will change unless voters get more involved in local affairs and elect politicians who are prepared to implement long-term so-

lutions that will keep taxes under control and tackle the infrastructure deficit in a rational, innovative and cost-effective manner.■

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Part 3: In Need of Reform

Guest commentary
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In need of reform

Canada needs a more standardized municipal service delivery regime. Municipal activities are similar across the country, yet business processes are often very different. As a result, Canada's 3800 or so municipalities waste billions of dollars each year on tailor-made products and services. Cost-effective, off-the-shelf solutions must be more widely used and conditions for the broad implementation of best practices and more competitive procurement must be created if municipal government is to become more efficient. Moreover, significant savings and economies of scale could be achieved if municipalities coordinated purchasing and operated more uniformly.

There is also a critical need to improve financial management and reporting and to provide elected local officials with the tools they need to address spiralling labour costs.

But the only way to implement real change and catalyse the municipal sector is through binding provincial legislation. This will make municipalities more sustainable and transform them into dynamic engines of local economic growth.

Binding legislation

Binding legislation is needed because leaving things to the discretionary authority of municipalities doesn't work. We all remember the spending on non-core infrastructure that was common during the heyday of the national infrastructure program. Another example are amendments to the *Ontario Municipal Act*, which allow municipalities to create new positions, such as auditor general and ombudsman, to enhance local accountability. Few local governments have acted on it because it is not a requirement, forcing citizens in some communities to petition for the establishment of these positions.

One good example of binding legislation is Ontario's Bill 175, the Sustainable Water and Sewage Act, 2002. This measure compels municipalities to assess the costs of water and sewer services and to recover the money needed to operate, maintain and replace them. Although this has lead to higher user fees, it has made Ontario's water and wastewater infrastructure financially and environmentally more sustainable. It has also provided consumers an incentive to reduce water use, thereby lowering the cost of future infrastructure investments.

Enforcement mechanisms, however, must be in place. It was recently discovered that city of Ottawa bureaucrats dumped $41 million from

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other departments into its water and sewer operations.

Legislation that required consideration of public private partnerships (P3s) would also be beneficial. This method of financing and delivering public services has proven its value around the world, fostering innovation and a higher level of public sector accountability. Canadians have spoken about P3s for decades but have barely begun to put them into practice.

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Off-the-shelf savings and smarter purchasing

A special report on technology and government in *The Economist* (February 16, 2008) shows how significant savings can be achieved when a municipality discards traditional approaches. By getting rid of its servers and using off-the-shelf software provided by Google, Washington, D.C., for example, was able to reduce its software costs by a factor of twelve – from $50 a month per employee to $50 a year. This illustrates the financial drag customized purchasing has on municipalities. Collectively, Canadian municipalities could reduce their IT costs by some $100-$150 million annually if they followed Washington's example, not to mention the additional millions that could be saved in needless consulting and maintenance fees.

Legislation must be enacted to help ensure more accountability, uniformity and innovation in the business processes used by municipalities. Contracts should be performance-based, with incentives for success and penalties for failure. Municipalities must more effectively transfer risk to the private sector, buy more shrewdly, and put an end to tenders that allow costs to escalate after contracts have been awarded. In most cases, tenders should simply define a service outcome and let the private

sector determine how to best achieve it. Finally, assessing the lifecycle costs of products must become a prime consideration in all purchasing.

Municipal accounting -- dramatic improvements needed

Another area that would benefit from framework legislation is accounting. Proper financial information is essential to effective and accountable management. A recent study by the Frontier Centre for Public Policy, *The 2007 Local Government Performance Index* (LGPI), found significant deficiencies in the accounting practices of Canadian municipalities. This makes it difficult to analyse the performance of our local governments, undermines the management of our infrastructure, and makes it impossible to grasp pension fund liabilities,




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which are incompletely and inconsistently reported. The lack of mandatory and basic accounting for infrastructure assets leaves Canada far behind international standards.

According to the Frontier Centre study, "One of Canada's best hopes for economic advancement could well lie within improving the competence of local government, more particularly their adoption of 'asset management' best practices…" It advocates the adoption of more competitive tendering, the reduction of union influence in work practices and the creation of more performance incentives for employees. Not surprisingly, the study showed "that a lack of core focus is correlated with higher municipal cost." It argues for "a consistent Canada-wide set of accounting standards and performance frameworks for municipal accounting."

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Flexible successor provisions

The constraints placed on municipalities regarding outsourcing are largely attributable to successor provisions. Broadly, these provisions under provincial labour codes require private companies to assume responsibility for all unionized public employees who are redeployed or transferred by outsourcing, or whose benefits may be affected. Though the right of municipalities in this regard has been confirmed in numerous court cases across the country, most current statutes contain far too many loopholes that enable unions to challenge outsourcing. Taxpayer-friendly laws that allow elected municipal officials more flexibility in outsourcing would be beneficial.

The pension bomb

As discussed, sub-optimal accounting practices make it difficult to determine the total pension liability in the municipal sector. We do know, however, that it is growing and unsustainable. Though greater use of outsourcing could help municipalities mitigate this liability, the retirement of a large number of highly paid unionized employees over the next decade will strain finances. Therefore, pension benefits must be scaled back now to deal with the effects of a contracting workforce and retirement age should be increased from 55 to somewhere between 60 and 65.

This is also a social justice issue. Independent inquiries should be established in every province to evaluate and compare the salaries of public employees with those in the private sector in an effort to ensure some parity. In addition to salaries, the range of employee benefits should be thoroughly examined and weight-

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ed, with special emphasis on pensions, so that comparisons fairly reflect the total wage package received by public employees. The two-tier world so often mentioned by unions has been finally created in Canada, and it is public employees who occupy the upper seats.

Toward better municipal government

Concerted legislative municipal reforms throughout the provinces will make local governments more effective, innovative and accountable. This will not only create economies of scale for existing products and services, but it will create new products and new processes as demand identifies new needs. Over the long term, this could become the foundation for public service delivery reform across all three jurisdictions of government, reducing duplication and overlap.

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The following might serve to inspire and guide some of the proposed legislation:

1. Make provincial and federal funding to municipalities contingent upon more outsourcing, improved accounting practices, competitive tendering procedures, greater use of P3s, group purchasing, etc., within a provincial and national framework;

2. Establish an independent procurement auditor responsible for the municipal sector in each province to enforce competitive procurement practices and handle complaints from suppliers. The municipal authority to exclude products and services from tenders must be abrogated.

3. Create an independent certification body in each province to determine which products and services meet municipal sector requirements. This will encourage the development of standardized products and services and drive down the price of municipal goods and services.

4. Reduce inter-provincial trade barriers and increase the number of suppliers available to municipalities by rolling out the Alberta-British Columbia Trade, Investment, and Labour Mobility Agreement (TILMA) across Canada.■

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