1.0 Introduction and Context

In the context of Canadian municipal public finance, user charges have been an important source of revenue for a long period of time. It is useful to provide a brief introduction to the context of local governments in Canada and the manner in which local governments are financed. Understanding the financing of local government is important in terms of policy implementation because in order for local governments to implement policies, programs, and projects, they must make budgetary allocations in their budget process, and in turn they must have appropriate revenue sources available in order to make the necessary allocations.

In addition to Canada’s central government, the country is divided into 10 separate Provinces. This division is important as first the British North America Act and later the Canadian Constitution reaffirmed that the responsibility for the creation and regulation of local governments is a provincial government responsibility. Consequently, each province has its enabling legislation in the form of a municipal or local government act as a central piece of legislation that is used in conjunction with other more specific types of legislation. As an illustration later in the paper references will be made to the Province of Ontario and its latest Municipal Act. Ontario is the Province with the largest population in which approximately one-third of Canada approximately thirty million people resides. It is also the Province in which the City of Toronto and the Greater Toronto Area, GTA, is located. The population of Toronto is approximately 2.3 million people, while the Greater Toronto Area has a population of approximately 4 million people.

There is some similarity in terms of the general approach to regulating local governments in Provincial legislation.¹ The similarity also exists for the municipal revenue sources for municipalities in all of the Provinces across Canada. There are three generally accepted classifications that represent the sources of revenue for municipalities across the country. These categories include the property tax, transfers or grants from senior levels of government, and what are referred to as “other revenues”. “Own source revenue” is

¹ F. Hoehn, Municipalities and Canadian Law: Defining the Authority of Local Governments, Purich, Sasakatoon, 1996.
considered to be the property tax and other revenues as these are revenue sources over which the local governments have some jurisdiction at least regarding the quantum that they wish to charge or collect. In 2000, 82.3% of municipal revenue was “own source”, with 53.3 % coming from the property tax and 21.3% from user charges. It is also important to note that almost all of the revenue obtained from grants or transfers comes from Provincial governments as in addition to the Provinces creating legislation; they are also responsible for providing transfer payments. In 2000 grant revenue comprised 17.9% of municipal government revenue of which 0.7 was from the Federal government. Some Federal government money flows to municipalities through federal provincial cost sharing agreements.2

The major revenue source for most jurisdictions across Canada including the Province of Ontario is the property tax. (53.3 % in 2000) The application of the property tax has a long tradition in Canadian provinces. It is based again on legislation that is specific to each province. In general however it is structured such that a tax rate is applied annually to an assessment base that is calculated as the sum of the individual assessments of all properties in the jurisdiction. Assessment is either undertaken by the provincial government, or by an agency or local governments in accordance with provincially determined norms and regulations. Each local jurisdiction, i.e. elected council, however would set the tax rate annually as part of its budget process.

However, as municipalities do not like to continually raise property taxes especially in election years, increasing use has been made of user charges as an own source revenue. Table 1 shows how this revenue source been increasingly used by Canadian municipalities over the last forty years.

<table>
<thead>
<tr>
<th>Year</th>
<th>Property taxes</th>
<th>User fees</th>
<th>Other own-source revenues</th>
<th>Total own-source revenues</th>
<th>Provincial and federal transfers</th>
</tr>
</thead>
<tbody>
<tr>
<td>1947</td>
<td>51.5</td>
<td>-</td>
<td>-</td>
<td>82.8</td>
<td>71.2</td>
</tr>
<tr>
<td>1955</td>
<td>53.4</td>
<td>-</td>
<td>-</td>
<td>77.1</td>
<td>22.9</td>
</tr>
<tr>
<td>1965</td>
<td>49.4</td>
<td>6.5</td>
<td>5.4</td>
<td>61.3</td>
<td>38.7</td>
</tr>
<tr>
<td>1970</td>
<td>43.8</td>
<td>6.3</td>
<td>5.0</td>
<td>55.1</td>
<td>44.9</td>
</tr>
<tr>
<td>1975</td>
<td>36.7</td>
<td>6.9</td>
<td>5.4</td>
<td>49.0</td>
<td>51.0</td>
</tr>
<tr>
<td>1980</td>
<td>35.3</td>
<td>12.2</td>
<td>4.1</td>
<td>51.6</td>
<td>55.2</td>
</tr>
<tr>
<td>1985</td>
<td>35.3</td>
<td>10.8</td>
<td>5.8</td>
<td>51.9</td>
<td>48.1</td>
</tr>
<tr>
<td>1990</td>
<td>36.9</td>
<td>12.0</td>
<td>5.4</td>
<td>54.3</td>
<td>45.7</td>
</tr>
<tr>
<td>1994</td>
<td>48.5</td>
<td>18.8</td>
<td>7.3</td>
<td>74.6</td>
<td>25.4</td>
</tr>
<tr>
<td>2000</td>
<td>53.3</td>
<td>21.3</td>
<td>7.5</td>
<td>82.1</td>
<td>17.9</td>
</tr>
</tbody>
</table>

2 An example of this is the Federal-Provincial Infrastructure Grant where approved capital projects are funded 1/3 each by Federal, Provincial, and Local governments.

It is important to understand the policy context within which local governments and particularly Ontario have been operating over the past fifteen to twenty years. To understand this context it is important to understand the large public finance picture in Canada. In the late 1980’s the Federal government became very concerned with the very large National debt where approximately 1/3 of revenue collected was required to pay the interest on the national debt. In an effort to move toward balanced budgets and reducing the impact of debt, the Federal government moved toward reducing the transfer payments that it gave to the provinces. The provinces in turn, many of who also had significant accumulated debt and annual budget deficits where now faced with declining transfers from the Federal Government. Their response in many cases was to reduce the transfers that they in turn gave to municipalities. This lead to municipalities having to make up the revenue reduction to maintain the range and quality of services via “own source revenues”. Consequently, municipalities had pressures to increase property taxes, and /or increase the quantum and range of user charges. There was a tendency and in many cases need to undertake both changes.

In the Province in Ontario, the response of the Provincial government was to undertake a number of policy changes in 1998. The most significant change in this context was called ‘Local Services Realignment’. This policy essentially eliminated transfers to municipalities, as we knew them in Ontario. In addition to eliminating the transfers, it also altered which level of government that was financially responsible for the services that citizens received. It essentially redefined which level of government would be responsible for each service. The outcome is often referred to as downloading financial responsibility for a broader range of services on local governments in Ontario. In order to minimize that impact of this reform on the property tax rates imposed on municipalities, the Province decided to provide funding for 50% of the residential component of education taxes. This provided “tax room” for municipalities to increase their component of the property tax without increasing the overall property tax burden of property owners.3

The general and Ontario context is important to understand as it leads to a motivation for increasing the use of user charges by Canadian/Ontario municipalities. As they need to increase revenue from “own source revenues”, elected officials do not like increasing property taxes especially in election years.

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3 In the Ontario property tax system both local governments and School Boards determine tax rates that are applied to assessed values of properties to finance the services that they provide. The local municipality will collect all of the property tax and then distribute it to the appropriate public bodies.
Consequently, applying new or increased user fees are an alternative they may have less of a political impact than increasing property taxes.

In order to better understand the application of user chargers the next section of the paper will discuss the rationale and theory by which user chargers may be applied. Comments will also be made on the impacts and potential limitations of applying user charges. The following section will describe the application of user charges in Canada and more specifically in Ontario as the Province in its recent new Municipal Act has created new regulations for the application of these charges. Finally, conclusions will be drawn about the Canadian/Ontario applications in the context of how user charges may by applied in the Central and Eastern European context.

2.0 Theory and Applying User Charges

With regard to economic principals there are two approaches upon which taxes are charged or revenues are raised: the “ability to pay principle”, and the “benefit principle”. With the ability to pay principle those who have greater ability or economic means should make greater contributions. Applying the benefit principle means that people should pay or contribute for a good or service in accordance with the benefits that they receive. It is the latter of these two principals, the benefit principle, that is the basis upon which user charges are applied. This application in itself provides insight into the type of services for which the application of user charges may be appropriate. It is those government provided goods or services where the beneficiary can be identified and consequently charged. Where a good or service has “public good” characteristics user charges may not be appropriate.

There are some generally accepted reasons for the application of user charges. First and foremost is that they promote economic efficiency in terms of the use of the good or service and allocation of public sector resources. This is important in local government as of the three economic functions of government, the efficient allocation of resources is the function that is central to local government. A second benefit is that it rations the use of the good or service. Rationing may take place by price or congestion. However, where price signals exist it provides insight to the providing government regarding how much of the good or service to provide for its residents. Local government decision makers in providing good and services have the annual problem when setting the budget in determining how much of a specific good or service to provide. The use of fees to replicate prices and the associated demand provide some insight for the decision makers at budget time regarding how much of a service to provide. This will help to promote the efficient

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4 The theory and applications are discussed in detail in a number of sources. For example, see Harry Kitchen, Municipal Revenue and Expenditure Issues in Canada, Canadian Tax Foundation, Toronto, 2002; and Donald N. Dewees, “Pricing Municipal Services; The Economics of User Fees”, in the Canadian Tax Journal, Vol 50, No. 2. 2002.

5 The three economic functions of government are the efficient allocation of resources, the redistribution of income, and stabilization policy, i.e. prices, inflation, employment and economic growth.
allocation of resources. Finally, user charges generate revenue for the municipality. This is important simply in terms of providing revenue to fund all or part of the provision of the service. In addition, the injections of this revenue may provide the government to either provide a higher level of the service than what would be provided in the absence of the charge, or a broader range of services for its residents. This leads to an enhancement in the quality and/or quality of services for residents. An example of this in the North American context is the use of user fees for recreation services or programs. When some revenue is generated from these programs, a municipality will then have the ability to provide a broader range of programs and services to its residents.

Once the decision is made to apply a user charge for a service because the beneficiaries of the service are definable, there is also the need to make a decision on how to calculate the charge or fee. If we wish to revert to the economic efficiency argument of economic theory, the argument would be made that the charge should be based on the marginal cost of providing the good or service where the cost includes both the operating and capital cost of providing the good or service. This ideal raises several questions with respect to determining the user charge. First, if it is possible the charge should reflect the marginal cost. In theory this is an excellent ideal. However, in practice it is very difficult to determine true marginal costs for a variety of reasons. Consequently, the fall back position is to base the charge on a determination of average cost. This approach is easier to undertake from a practical perspective.

In attempting to apply either marginal or average cost pricing to the user charge a decision has to be made regarding which costs to include in the calculation, capital costs, operating costs, or both. Obviously to apply full cost pricing, both or all costs should be used in the calculation. However, there may be circumstances when only one of the two cost components is appropriate to be used in the calculation for the user fee. For example, there could be a situation where the capital costs for transit are provided by a grant from senior levels of government. If the objective of a user charge transit fee is cost recovery for the charging government unit, then the charge would only reflect the operating costs. On the other hand when municipalities impose charges for growth related capital costs, the quantum of the charge would only be based on capital costs with the operating costs being borne via property tax revenues. There are also examples such as those often applied for the provision of water in which both the operating and capital costs may be used calculate the charge. There may be situations or policy decisions where there is a desire to determine charges not only for the purpose of revenue generation but to meet some additional policy objective. This may lead to variations on the pricing applications. These pricing applications include peak load pricing, geographic variations, differentiation by user, and the inclusion of externalities in the pricing.

Peak load or time related pricing refers to varying the price charges in a temporal fashion. The idea is to charge a higher price when there is peak demand for the specific service. In this way the higher price will lead to a reduction in demand for the peak period, and people will be enticed to use the service during non-
peak periods. The benefit from this approach is that the infrastructure or capital needs for the service will not have to provide as much capacity as would be required without this pricing approach. Consequently, less expenditure is required for capital/infrastructure expenditures. Furthermore, better use of the capital/infrastructure is encouraged when it would otherwise be underutilized.

Another variation in user charge pricing for some services is to vary the charge by geographic location. This can be the result of applying one of the earlier identified pricing rules, or be the result of a policy decision to try and alter the user fee by geographic locations. In the first instance where costs of providing a service vary by location, one might expect charges to vary by location. For example providing sewer and water services to a remote location will result in a higher charge than providing the same services contiguous to existing development where services are already being provided. An alternative approach would be to apply different charges in various locations in such a way not to accurately reflect the cost of service provision but to achieve some additional policy agenda. Higher charges could by applied to certain areas to discourage development of low charges may be used to encourage growth and activity in certain areas.

It is also possible to alter the application of the charges based on the type of user for a specific type of service. For example, it may be desirable to set lower charges on some fees for certain groups of users. Some recreation programs or athletic rental fees may be set lower for certain groups such as children or youth as compared to adults. Adults who are income earners may be expected to pay higher rental fees for ice time in areas to play hockey relative to youth groups. This reflects the groups’ ability to pay or recognition of the need to provide athletic facilities to youth and children. Other variations in the application for different groups could relate to different charges being set for senior citizens or adult groups. There could also be differential charges applied to different members by obtaining and understanding the need to alter the charges various income levels.

Another variation would be not to only include the actual private costs, however they are defined, but also include any social or external costs that are also present in the need and or delivery of the good or service. This is a more theoretical approach that takes into account the economic concept of externalities. An example of these costs not being taken into account is the case when there was the need to rationalize user fees when the New City of Toronto was created by the from seven local government units. The new city undertook a study to determine the appropriate user charges that previously were set differently in each of the seven jurisdictions. One of the results was that some of the recreation user charges increased or now were imposed for certain programs and facilities. In the old City of Toronto many of these programs were previously free. With the new charges in the old city there was a noticeable increase in mischief problems

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with teenagers in the inner city (old City of Toronto area). Critiques of the new charges indicated that with teenagers unable or unwilling to pay the new fees to participate in the old program, they were now imposing increased policing costs as they wandered the streets in groups. The argument could be made from an economic perspective not that the user charge should be eliminated, but rather that it was set incorrectly, i.e. too high, as it didn’t take into account the external costs, i.e. increased policing, resulting from the new charge.

A useful typology to user charges has been suggested by Richard Bird that may be useful in helping policy makers to categorize user charges and then ultimately set the charges at appropriate levels for their specific jurisdiction. He identifies three types of user charges; service fees, public prices, a special benefit charges. Service fees refer to payments made for licenses, permits and permissions that are already required by law. Examples include building permit fees, vendor’s permits, as well as marriage and dog licenses. These tend to have the charges set on a cost recovery basis depending on the cost of providing and/ or administering the service. The point is that for items that fall into this category, municipalities should ensure that the charge that is being collected covers the cost of providing the service.

Public prices on the other hand refer to revenue generated from goods or services provided by the public sector, local governments, that may also be provided by the private sector. The “prices” should be set at a competitive level and not include any special tax or subsidy level in them unless it is necessary to promote efficiency. Examples of public prices include public utility charges, admission charges to recreation facilities, and transport charges.

The final category is special benefit charges. These reflect charges that are compulsory payments to support local revenue whereas the previous categories tended to be voluntary. These charges support specific benefits that tend to support specific residents often by bestowing benefits on the properties owned or occupied by these residents. Examples include special assessments or improvement taxes, assessments for business improvement areas, and items that relate to developer exactions such as development charges (impact fees in the US). Most of these charges are imposed or related to property and are determined based on assessment or some measure of property characteristics.

With the increasing application of user fees in Canadian municipalities, local government decision makers should be gaining a greater understanding in terms of their applications. It is also important for them to understand the impacts and limitations of their applications. Although user fees rate high in terms of efficiency, there are questions with user charges regarding their impact on equity considerations. The most important equity impact of user charges is the fact that they are regressive in nature and consequently place

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greater burdens on lower income individuals and households. For some types of user charges there have been attempts to minimize the regressive nature of user charges especially for those applied to recreation facilities and programs. This has been achieved via providing vouchers for low-income households for programs by applying differential fees for various groups. An example is lower fees for renting ice time for youth groups relative to adults. There is also an example in the area of transit fares where lower fares are set for students and senior citizens.

It is important to ensure that in designing user charge systems or programs, policy makers take into account the type of user charge. They need to undertake an analysis of the cost or pricing rule to be applied to the type of charge, and an analysis of the impacts of the charges.

3.0 Application in Canadian Municipalities

This section will provide some examples of the applications that have taken place in Canadian municipalities. They are organized using the typology suggested by Bird referred to earlier in this paper. This typology is helpful to municipalities in considering how to approach the application of user charges when designing their pricing approaches.

3.1 Service Fees

In explaining the Canadian applications the focus will be the Province of Ontario as an illustration. As mentioned previously, it is the largest province in terms of population and also has the largest urban area, the Greater Toronto Area. It has approaches that represent the current state of Canadian practice in the area of user charge applications. As was previously indicated and shown in Table 1 the use of municipal user charges has been increasing. In the Ontario context user charge applications have been supported in terms of clarifying the rules for their application by the Province’s most recent Municipal Act. This replaces an Act that has not been revised in a comprehensive fashion since its inception. Some examples may also be provided for urban type service charge applications that are not directly under the jurisdiction of local government in Ontario. These examples are interesting applications that provide some interesting lessons or potential applications for other jurisdictions.

If we first consider the type of user charge applications that Bird refers to as service fees we can note that Canadian municipalities have a long history of applying these types of user charges. This is especially true for the activities of planning and urban development. In the Canadian land use and building system permits, various types of permission are required to make changes in land use in planning system. Each province has legislation that enables municipalities to control land use through the use of official or master plans, changes in zoning bylaws, and the permission to subdivide or create new lots upon which building may
occur. After ensuring that the appropriate land use provisions are met, property owners must obtain a building permit in order to construct their desired building. All of these activities, changes in land use designations, creation of new building lots, and obtaining building permits require the applicant to pay a user charge.

It would appear by examining the results of a survey of municipal user charges in the late 1990’s, and the authors experience in research and consulting with local governments in Ontario that there was not a uniform or always rationally calculated approach to determining the planning user charges applied by Ontario municipalities. It would appear however, that the larger, more growth oriented municipalities that have more activity in this area have higher charges that may reflect a more careful calculation of charges relating to the cost of the service undertaken by the fee. However, the survey results show wide variation for the responding municipalities. For example, fees for applying for amendments to the Official (Master ) plan ranged from $250 to $4,470 with the median being $1000; zoning by-law amendments ranged from $200 to $1,750 with the median being $800; and subdivision applications ranged from $100 to $5000 with the median being $1,000.9

This demonstrates a wide variation and the lack in many cases of any widely applied pricing rule to guide the calculation of the charge. However, ideally the charge should reflect the cost of the work by the municipality in processing the application. Although, no comparable survey exists for user charges after the imposition of the new Municipal Act, there is some indication that the municipalities, especially in high growth areas have undertaken some calculations regarding the cost of undertaking these planning functions to guide the current setting of their charges.

Another example is with regard to building permits. In this case the cost to the municipality is not only the issuance of the permit, but also the cost of the building inspectors actually inspecting the construction to ensure that it is being undertaken in accordance to the Ontario Building code and local land use requirements. These fees are typically calculated based on the estimated value of the building construction. This presumably reflects the time and complexity of the inspection requirements. An illustration of these fees is also provided by the 1997 survey. It found that the fees for a 1,500 square foot residential unit would range from $72 to $1,470, with the median being $734. Once again, this variation demonstrates a wide range of possible ways in which municipalities determine their fees. Some may have had the same fee for numerous years and have just kept it the same, others sometimes check what neighbouring municipalities

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8 Changes to the zoning by-law may include not only change in land use, but changes in density, the building envelope or other items controlled by zoning such as required, parking, building setbacks, or landscaped open space requirements.

are charging, and some may actually attempt to calculate the time and consequently cost of undertaking inspections. This last approach and analysis should be undertaken.

In addition to these types of planning/building related service charge fees, many additional examples could be given. There are other examples in the Building and Planning Departments such as demolition permits and other types of zoning by-law fees, and there are numerous examples in other departments of Ontario municipalities. These include items such as business licenses, peddler’s licenses, taxi licenses, marriage licenses, amusement licenses, plumbing permits, burning permits, parking permits, etc.

3.2 Public Prices
Applications of user charges to reflect public prices in the Canadian and Ontario context are best illustrated by charges for utilities, recreation fees, transit and potentially road pricing. The first of these categories is utility pricing that in the local government context will generally include water and hydroelectric power, and in some municipalities includes gas as a utility provided for heating buildings.

If we examine pricing for water services in Canadian municipalities there is a wide range of pricing approaches that are applied. However, it is desirable for municipalities or authorities that supply this service to set the water rates that reflect the costs of the service provided, and charge in such a way to achieve or promote economic efficiency. The first step in this process is for municipalities to ensure that the price that they set per liter or gallon reflects the full cost of providing the service. This requires including both the operating and capital costs. It is necessary to undertake full life cycle including replacement costing for facilities. This has not always been historically undertaken in Ontario or Canadian municipalities. However, in Ontario in response to a major problem with water quality that resulted in severe illness and death in the Town of Walkerton, Provincial legislation has been passed that requires municipalities to set rates that reflect the full cost, operating and capital of providing the water to its users. The objective is to ensure that enough revenue is generated to ensure water quality via testing, treatment, and appropriate infrastructure.

Once the municipalities or authorities take the full cost into account, the question of how to charge the users still exists. The ideal is to apply marginal cost pricing. To apply this approach it is necessary to have the water metered at each unit so that each unit will pay for the water that it actually uses. In the absence of metering, municipalities have used proxies such as the number of bathrooms in the house/building or the size of structures. There are also variations in residential and commercial rates. Commercial rates across Canada use a broad range of pricing approaches including constant unit rates, declining block rates, increasing block rates, humpback block rates, seasonal rates, excess use rates, and mixtures of the various

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10 This approach is advocated by economists for efficiency. For example see Donald N. Dewees, “Pricing Municipal Services: The Economics of User Fees”, in Canadian Tax Journal, 2002, vol. 50. No 2.
Whether applying the more complex commercial rates or more straightforward residential rates, it is important to have the water metered so that people will pay the costs of what they use. This will encourage people to conserve water and promote efficiency. Unfortunately metering of water is not undertaken in all jurisdictions across Canada. It was reported in 2002 that residential units were metered in only 43% of all Canadian municipalities and commercial users in only 58%. Despite the fact that most of the lack of metering tended to be in municipalities with populations under 50,000 people, there were also some large cities including Toronto, Calgary and Vancouver that lacked metering in some districts.

There is substantial evidence from Canadian applications that installing meters leads to a reduction in water consumption. Table 2 below shows the results of a number of studies that support this outcome.

**TABLE #2**

<table>
<thead>
<tr>
<th>Municipality</th>
<th>Effect</th>
<th>Date of study</th>
</tr>
</thead>
<tbody>
<tr>
<td>Etobicoke, Ontario</td>
<td>Water use was 45% higher in unmetered areas than in metered areas of comparable assessment.</td>
<td>1972</td>
</tr>
<tr>
<td>St. Catherines, Ontario</td>
<td>Consumption dropped by 11% following metering but rebounded because prices were kept low. Two years later, water usage was higher than before metering.</td>
<td>1967</td>
</tr>
<tr>
<td>Alberta</td>
<td>10 to 25% drop in water use following meter installation</td>
<td>1984</td>
</tr>
<tr>
<td>Peterborough, Ontario</td>
<td>10% reduction in water use predicted following meter installation.</td>
<td>1984</td>
</tr>
<tr>
<td>Calgary, Alberta</td>
<td>Unmetered water use was 46% greater than in metered residence.</td>
<td>1984</td>
</tr>
<tr>
<td>Calgary, Alberta</td>
<td>Unmetered water use was 65% greater than in metered residence.</td>
<td>1978</td>
</tr>
<tr>
<td>Canada, selected municipalities</td>
<td>Residential water consumption was twice as high in unmetered communities as in metered communities.</td>
<td>1975</td>
</tr>
<tr>
<td>Port Elgin</td>
<td>25% reduction in overall demand after metering.</td>
<td>1991</td>
</tr>
<tr>
<td>Small municipalities in Ontario</td>
<td>The impact of metering is evident in the 1996 water municipal use data compiled by Environment Canada. Average per capita water demands for metered and un-metered communities indicate that metering leads to a 22% reduction in average daily water flow per capita and a 27% reduction in maximum daily water flow per capita. An analysis of the residential water use component of total demand using the same 1996 database indicated that metering causes residential demand to fall by about 30% in small and medium sized municipalities and 20%</td>
<td>2000</td>
</tr>
</tbody>
</table>

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12 Harry Kitchen op cit page 138
in large municipalities.


The results in the table show a consistent pattern that over a more than twenty five year period and for a range of municipalities of various sizes metering the use of water has lead to a reduction in the volume used.

Similar applications and analysis apply to other utilities such as hydro and natural gas. These may be supplied via municipalities or public authorities that are often controlled by a government body. An interesting potential hydro efficiency application has been suggested by the Premier of Ontario. He is advocating the use smart hydrometers that will differentiate prices via peak and off-peak consumption. This application has the potential to lead to efficiency and a reduction in consumption.

Recreation user fees have a long-standing application in Canadian municipalities. These fees or charges range from programs such as swimming lessons, tennis and skating lessons, summer camp programs as well as renting facilities like hockey arenas, swimming pools, and athletic facilities. As many of these have private sector competitors, the pricing and quality of service may have an impact on demand. For these activities there has been some attempts to set the charges both to address efficiency and equity issues. However, these have been limited to a small range of charges. For example, the renting of ice time in municipal hockey arenas is often differentiated by higher rates for peak times relative to off peak. Furthermore, often the rental rate is different for youth renters as compared to adults. In some cases vouchers or reduced rates for some programs are applied to lower income households or individuals. There also may be reduced rates for seniors or youths in some programs and rentals. This has been demonstrated in the Municipal Finance Officers of Ontario 1997 user charge survey. It is indicated that the median adult ice rental time was $97/hour for peak time compared to $70 per hour for off peak. The median hourly rental rates for youth were $70 peak and $58 off peak.13

With respect to transit user charges, the relative rates in Canada tend to be higher in Canadian municipalities as there is no general federal funding or subsidy for mass transit in Canada. There tend to be variations in prices for some users such as students and seniors, an incentive for frequent users via monthly pass rates that provide a discount. However, there is not a tendency for Canadian systems to apply fare by

distance pricing that would support pricing based on marginal cost pricing. There is however, multiple zone pricing in some jurisdictions that is a crude attempt at this pricing approach. There are other transportation related charges that might be considered in the context of user charges that may be used in conjunction with approaches to transit pricing to address some overall policy regarding transportation in urban areas. These are user charges that relate to private auto usage. For example, governments may apply user fees as a form of road pricing. The best know recent example of this is the London 10 L charge for driving into the City. The recently elected mayor of the City of Toronto discussed imposing a similar charge in Toronto for cars driving on major expressways into the city. There is already a limited access highway, 407, at the northern edge of Toronto that is North America’s first electronic toll highway. The toll is charged by scanners recording the users’ license plates who are then sent a bill in the mail for their use of the highway. The amount charged is based on distance traveled and whether they used the highway at peak or off-peak times. In addition to road pricing, municipalities may set parking charges for municipally owned parking lots to reflect peak pricing approaches to discourage people from driving cars into the urban core.

In this section some examples of the Canadian and Ontario applications of user charges as public prices have been provided. This has not been a comprehensive detailed list and discussion, but rather one to illustrate several applications and issues.

3.3 Special Benefit Charges
A good example of special benefit charges is the application of what are known in Ontario as Development Charges. Variations on this application also occur in two other Canadian provinces, British Columbia and Alberta. In U.S jurisdictions, they are what are typically referred to as “impact fees”. These are charges placed on new development to pay for the offsite growth related capital costs related to the new development. They may be imposed for both residential and nonresidential development. The premise is the benefit principle in that growth should pay for itself in terms of its requirements for capital facilities. Existing residents and businesses should not be required to subsidize the costs of growth.

Ontario, has had various applications of development charge type fees going back as far as the 1960’s. However, the way that they were applied and calculated by municipalities in the years prior to the first enabling legislation was not based on any rational pricing rule. Consequently, there were many legal challenges to their application.  

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14 Frequent users have the alternative have the option of purchasing a transponder which records the billing without scanning the license plate which leads to a lower administrative charge being included in the billing.
With the passing of the first legislation, The Development Charges Act 1990, there was not the legislative basis for defining the growth related capital costs that could be included in the charge and a defined method by which the calculation could be charged. The legislation permitted the inclusion of all growth related capital costs based on an average cost calculation of projected population growth and its related development.

Later applications and revisions to the Act lead to the use in some jurisdictions of “area specific development charges” which permitted variation in the charges based on different cost of engineering/works related services in various geographic areas. This meant that the charges in these cases were attempting to move beyond average cost calculations to a variation of marginal cost pricing. From an efficiency perspective, this is considered to be an advancement over the previous applications. However, the new legislation also limited the range of capital cost that could be included in the calculation by reducing the range and/or discounting the amount of people or soft service capital costs that are included in the calculation. Although there is general agreement regarding the inclusion of property related services in the cost calculation, there can be some debate among interested parties regarding which and how much of the people related capital costs should be included.\textsuperscript{16}

It important to note that much of Ontario has two tiers of local government. In addition to what we refer to as local municipalities, we also have regional governments or counties that provide a range of services. Under the development charge legislation both levels of local governments can impose development charges for the services that they provide. In addition, School Boards may impose development charges for the capital costs of new schools required due to growth. Consequently, as an example, the combined charges that are imposed in some of high growth jurisdictions in the greater Toronto area are in excess of $15,000 for a single-family residential unit.\textsuperscript{17}

This application meets the objective of providing necessary revenue to municipalities, and not having the costs of growth imposed on existing taxpayers. The alternative to these charges is raising the property tax. The use of the charge will however promote economic efficiency. The charge approach is desirable not only because it has moved beyond simple average cost pricing to a variation of marginal cost pricing in its application, but it also represents a form of multi-part pricing which is deemed to be very efficient. Its multi-part application consists of offsite capital costs that are paid for by development charges sometimes based on a marginal cost variant, the connection fee to the services is born by the developer as they are required as part of subdivision agreements to provide all services internal to the subdivision at existing municipal standards, and the operating costs for the services are paid for by the property taxes.

\textsuperscript{16} The people related service include such facilities as libraries, sport facilities and areas fire stations, cultural facilities and expansions to municipal offices i.e. City Hall’s.

\textsuperscript{17} For example, half of the eight municipalities in York Region, the high growth area north of Toronto have single family detached charges greater than $15,000. See Urban Development Institute, “Government Charges that Drive Up Housing Costs: A Study of Taxes, Fees, & Charges in the GTA”, 2002.
There are other applications of special benefit charges such as the local improvement charges and special assessments for Business Improvement Areas each of which has legislative basis for the application and use of the charge and its revenue. However, the development charge application was provided as an illustration as it is the largest revenue source in this category and it provides an example of how the legislation was necessary to ensure the improved application of the use of this type of development charge. Furthermore, the legislation ensures accountability in the actual use of the revenue for the purposes for which it was collected.18

4.0 Conclusion
Over time Canadian and Ontario municipalities have made increasing use of user charges a source of revenue to finance municipal services. It is important to be aware that residents have demand an increased range and quality of services. This coupled with a reduction in transfers and expectations that municipalities finance a greater range of services has provided the impetus for their increased use. Over time municipalities have also become more sophisticated and better in terms of making use of pricing rules and applications that enhance efficiency, and address some of the equity issues associated with applying user charges.

A major part of the impetus for better and more efficient approaches to user charges may be attributed to Provincial legislation. In Ontario, this includes the new Municipal Act passed to become in force in January 2003. Although the old act made provisions for the application of user charges, the new Act has more specific regulations including the requirement that a master list of fees be reviewed annually as part of the budget process. There is also legislation that requires municipalities to set sewer and water rates that reflect the full operating and capital cost of providing the service. Finally, earlier, i.e. in the 1990's development charge legislation and the revision to it clarified that way in which development charges were to be calculated according to the new provincials rules. Therefore, a key component to improvement in the municipal user charge system was legislation that provided the framework for municipalities to design and apply a user charge system that is consistent and rational, i.e. based on sound pricing applications.

As one of the main benefits in making more extensive use of user charges is economic efficiency, this has to be considered in the context of the equity impacts that potentially result on lower income households and individuals. Taking this into account local government decision makers have to decide when and how to apply user charges. As indicated above in the Canadian experience, enabling legislation with appropriate regulations and requirements is an important precondition for an effective and appropriate user charge
system. This also requires knowledge and training for local officials regarding how to implement the legislation and design the charges.

The municipal finance situation in Central and Eastern European countries is different than in Canada where property tax revenues are the largest source of revenue. Here decision makers have opted for the use of user charges to finance some local services rather than increasing property taxes. This has proven to be more politically expedient than raising property taxes and has the “benefit principle” advantage of efficiency if appropriately applied. In the Central and eastern European context, rather that user charge revenues being a substitution for property tax revenues, user charge revenues serve as more of an expansion of local source revenues to enhance transfers from senior governments. Consequently, the Canadian benefit of user charges, i.e. mitigating property tax increases is not as relevant in the European context.

Therefore the prime rationale for the application of user charges is the expansion of the range and perhaps quality of services, as well as promoting of economic efficiency in service provision. Again, the charges must be applied with the equity impact tradeoffs considered. This means either applying the charges for services that equity impacts are not a major consideration; or designing the charge to minimize the regressive impacts. Hopefully the Canadian applications and impacts described in this paper are instructive in providing some insights regarding the approaches that have been successful as Canadian municipalities have expanded their use of user charges over the years.

**Bibliography**


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18 The legislation requires that development charge revenue by placed in special “earmarked” funds and furthermore that annual reports by made to the Province regarding the use of these funds.


