Although municipalities fall within the exclusive jurisdiction of the provinces, revenue powers and expenditure responsibilities have been delegated to them by the provincial governments which make their financial position an integral part of the whole provincial picture, and consequently, to that extent, of Dominion-provincial relations. The major functions of education, public welfare, and highway construction are shared, in varying proportions, by provinces and municipalities; the whole field of revenue powers left to the provinces is divided, on the average about equally between provinces and municipalities, although the proportions as between provinces vary greatly. The part played by municipalities in taxation (in 1937 municipalities raised 31 per cent of combined Canadian governmental revenues from all sources), and in expenditure makes it essential to consider them in any review of the Canadian public finance system. For this reason the Commission has considered jointly provincial-municipal revenues and expenditures wherever appropriate. The exclusive jurisdiction of the provincial governments over municipal affairs has, however, been recognized throughout, and the distribution of benefits arising from the Commission’s recommendations in Plan I, although these benefits were calculated on the basis of the combined provincial-municipal position, is left entirely in the hands of the provincial governments.

Nevertheless, certain aspects of municipal organization and of municipal taxation and expenditure affect the financial position of the provinces and Dominion-provincial relations, and in this chapter they are discussed from these points of view.

I. THE BACKGROUND

At Confederation only rudimentary municipal organization existed outside of Ontario, and in spite of the hope of the Fathers of Confederation that local government would develop quickly in the other provinces and assume some of the burdens of the financially over-loaded provincial governments, growth, particularly in the Maritimes, was very slow. Consequently, from the very beginning there existed a great disparity between the different provinces in the proportionate distribution of provincial and municipal functions. As provincial revenues, on a per capita basis, were roughly equalized by the subsidy system initially adopted, variations in the weight of taxation, and in the government services provided, depended largely on the degree of municipal development. Because of the additional taxation involved, municipal development was opposed in Quebec and the Maritimes, while in Ontario well-developed municipal agencies imposed heavier taxation and took a commanding lead in educational and railway and road expenditures.

The Prairie Provinces established a checkerboard municipal system covering virtually the whole occupied area as rapidly as their settlement permitted; in British Columbia only one-half of 1 per cent of the area (containing 75 per cent of the population) has been municipally organized—a striking illustration of the localization of resources and the physical peculiarities of that province. Prince Edward Island, small in area and population, has required virtually no municipal machinery.

From these diverse circumstances, and accidents of time and place, the present heterogeneous collection of municipal systems arose. The variations from the complex and overlapping multiplicity of units in Ontario and Quebec to the geometric, if not economic, regimentation of Prairie units, and the limited local developments in the Maritime Provinces and British Columbia, have important implications for provincial finances.

Even more important than the variations between provincial systems is the great and increasing spread between kinds of municipalities. Metropolitan centres, tiny hamlets, and sparsely populated rural areas are all known as municipalities. It is obvious that their problems must differ greatly in degree and in kind. We cannot, in fact, speak of the municipal problem; there are municipal problems characteristic of certain regions and of certain provincial systems, problems characteristic of certain types and classes of 

municipalities, and problems associated with individual municipalities in special circumstances. The particular revenue, expenditure, or debt factors which may be of dominating importance in one case may have little relevance in another, and sweeping generalizations are thus of very limited utility. In no field is local knowledge and responsibility more important for successful administration. This is an additional reason why the Commission in recommending National Adjustment Grants has not suggested any Dominion conditions or supervision governing the expenditure of these grants, or their division between provincial and municipal governments.

Nevertheless there are some developments which have affected all municipal governments, although in diverse ways and frequently in such a manner as to widen the existing differences. This is important, because to the extent to which a generalization can be made as to what is the municipal problem in Canada, it is that wide differences exist between municipalities in ability to support their responsibilities. Since Confederation local political units have been saddled with more and more economic functions, and have become less and less economic units.

Up to the end of the last century Canadian municipalities were, much more than now, the local units in the economy; their people were more on a subsistence, and, therefore, a self-sufficient basis; and the functions of municipal governments were local in the most direct sense of the term, largely arising in every case out of the particular circumstances and desires of the community. Municipal boundaries were more justifiable—each town was a clearly recognizable entity, and rural areas were more than now separate and distinct regions, each with a more highly developed local character. Trade was chiefly between the town and its rural hinterland. Industrial activity was not great and mass-production manufacturing was unknown. Industry was dispersed, and within each community small factories, mills and home handicraft provided most non-agricultural goods. There was a frontier to be pushed out by the discontented or those unable to prosper, as prosperity was then known, in their original area. Occupations required little training or education, and training for one was adequate for many others.

Both the local consciousness and the absence of marked economic differentiation or interdependence between local areas, as well as the relative simplicity of the whole economy, were conducive to the concept of a separate local government for each area; each looked after its own affairs and was not greatly interested in or affected by the affairs of others. Education, roads, maintenance of local law and order, care of the poor, elementary sanitary measures in towns, and the provision of a few communal facilities were, in such conditions, the natural functions of local government.* They were capable of being completely decentralized, and were roughly within the capacity of every local unit to provide. In any case, if inequalities existed, they were simply the result of differences in the ability and ambition and good fortune of the local inhabitants and the stage of development from pioneer days. Such inequalities were of little concern to the province as a whole because they involved services which did not affect the general interests of the province, but were, to a very large extent, of purely local importance.

With the growth of the economy, boundaries between local units became less justifiable, but for purposes of local organization they were not inappropriate prior to the advent of the motor car. The optimum rural area was presumably that traversable by horse in a day, and it did not matter if boundaries were arbitrary lines drawn in accordance with the system of landsurveying, as in the case of most Ontario townships, and of many rural municipalities of the Prairie Provinces. The primary economic functions of government were land settlement and development, and the encouragement of industry, all of which were undertaken by the senior governments of province and Dominion. Social services and economic activities played a small part in municipal government, and could in those days have been considerably extended without putting strain on the municipal structure. Education, largely a local responsibility, was still conceived of in very simple terms. The neighbourhood was both the political and economic unit, and was capable of taking care of its own affairs.

The neighbourhood,—the local area in which each inhabitant knows a large number of the others and is conscious of a considerable community of interest with them,—must always remain a unit of local government, outside of large cities, but economic and social conditions have so changed that the number of matters of peculiarly local concern is restricted, whereas the field of governmental activities is widening. New functions of

* Education was somewhat of an exception since in all English-speaking provinces school districts, at least in rural areas, were not coterminous with local government units.
government cannot be efficiently or fairly divided among a large number of small areas, and some of the old functions have become inappropriate to the municipal sphere.

The great expansion in foreign, interprovincial and inter-municipal trade, and the accompanying increase in economic specialization even among municipalities, have made the economic welfare of one unit dependent on that of others, to say nothing of the outside world. An entire city may be dependent on the production of motor cars, a whole rural municipality on one type of agriculture, whether it be tobacco, fruit, wheat or live stock. Over much of the country each unit is producing primarily for "export" to other units, if not abroad, and imports from others most of its requirements.

The development and widespread use of the motor vehicle have created a need for highways, have enlarged the physical motor vehicle have created a need for economies influenced trade, relative municipal development, and the size of the area which can be described as suitable for local government. The trend of land values has in many cases been abruptly altered by the advent of the motor car; the development of cities at the expense of nearby towns, and of suburbs at the expense of cities, vitally affect municipal finance.

Industrialization, the greater complexity of all forms of economic activity, and advancing standards of every description, require an educational system which will give to the largest possible proportion of the people the best possible education. New knowledge with respect to the value of public health services, and the social cost of disease and poverty, have increased the interest and activity of the state in matters of health and public welfare, working and living conditions and wage levels.

Such social and economic changes necessarily affect the nature and scope of municipal government and central government alike. The general tendency to leave the responsibility for conditions within its own area to each municipality, both administratively and financially, and to require new functions of government relating to economic conditions to be undertaken primarily by local government areas whose boundaries are less and less those of balanced economic communities, has created many difficulties and anomalies in the municipal structure. These may be classified under three heads.

In the first place, many local government units are no longer the appropriate areas for governmental purposes of any description. This is particularly true of large cities, and of many rural municipalities in the Prairie Provinces. The case of the metropolitan area is conspicuous. Many people in such areas work in one municipality and live and pay taxes in another. The idea of the municipality as a community of neighbours has been necessarily lost in large cities at least, and the required standard is that of an efficiency which cannot be achieved when five or ten separate governments operate in a single integrated urban area among people who are economically interdependent; nor can the maximum economic welfare of the whole be expected if there are a number of widely varying tax-rates, standards of education and health measures and the like. Likewise in rural areas, the motor car is in process of rendering obsolete old municipal boundaries based primarily on the cruising radius of the horse. The motor car has extended the possible physical area of rural municipalities beyond the maximum desirable from the point of view of maintaining the identity of the neighbourhood. The boundary of a "neighbourhood" is now limited, not primarily by distance but by the other factor, always important, the number of inhabitants. Particularly in Western Canada, where settlement is sparse, municipal areas require extension for purposes of efficiency and economy, and this can now be done without sacrificing the local character of municipal government. It is in the extension of boundaries and in the pooling of costs as between complementary areas that is to be found one of the remedies for the social service costs imposed by transiency on certain unfortunate municipalities.

Secondly, even with adjustment of areas, modern conditions render desirable a large measure of co-ordination between municipalities, in their own interests, with respect to a number of their functions. The police department of one town must take cognizance of a crime committed in another fifty miles away within an hour of its occurrence. With the large and continual movement of people from one area to another maintenance of health services in one municipality is vitally affected by conditions in another. Particularly in rural areas the bringing of hospitals and other necessary institutions up to modern standards is a matter of co-operation between the municipal units concerned, or between the municipalities and the provincial government.

Thirdly, in the case of a number of governmental functions requiring large expenditures
(some of which were originally purely matters of local concern and, therefore, the subject of municipal responsibility, and others of fairly modern origin or at least development) the long-run interest of the province conflicts with the existing system of requiring the separate municipalities to find the necessary moneys. This system results in unfair inequalities between municipalities, in failure to maintain uniformly the desirable provincial standards, and in severe strain on the finances of many municipal governments. Modern economic conditions have tended to increase differences which have always existed between municipalities in wealth and tax-paying capacity, and likewise in the expenditures necessary to fulfil certain functions. Very often the poorest municipalities require the greatest expenditures on the services in question. So far as such expenditures are forced on the municipality by provincial legislation, as in the case of some hospital aid and child welfare statutes, the situation is obviously inequitable. An extreme instance is unemployment where the degree of expenditure is affected by provincial or nation-wide conditions and by provincial or federal policy; the municipality in this case is unable to control the amount of the expenditures which it is forced to bear, and its capacity to pay is restricted by the same conditions which render the expenditures necessary.

With respect to matters of admittedly local concern it is obvious that wealthier municipalities always will be able to supply their inhabitants with better services than poorer ones. But it is equally obvious that great inequality among municipalities is inimical to the maintenance of any uniform or minimum provincial standards. Some matters which were once of merely local interest cease to be so because the increase in disparity of wealth prevents the maintenance of approximately uniform standards. Matters of more than local interest should not and cannot be left to a major degree in the field of municipal government. In so far as they remain a municipal obligation the interests of the province as a whole are injured by the sheer inability of some municipalities to raise the same revenue as others either in proportion to population or to the amount of expenditure required, as well as by obstacles to provincial uniformity arising from the deliberate adoption by a municipality of a lower standard than that desired as a matter of provincial policy.

From what has been said it is clear that aggregate municipal figures are of very limited use in analysis of the problems, since the totals conceal the very disparities which create the chief difficulties and inequities. Valid comparisons could only be made and valid generalizations reached after each municipality had been considered separately, in the light of its own particular circumstances. Yardsticks and tests which are applicable to one may be completely irrelevant or misleading when applied to another. A municipality dependent on a single industry differs fundamentally from another of the same size engaged in more diversified economic activities. A Prairie city dependent upon agricultural conditions cannot be compared with an average industrial city in Ontario or Quebec, nor a pioneer community with a mature one. The greatest obstacle, however, is the dearth of statistics, and the lack of uniformity in those available. In some provinces current and capital items in municipal accounts are not distinguished in so far as their statistical presentation is concerned; in others, statements of aggregate municipal finances combine statements compiled on the accrual basis with others on the cash basis. An analytical breakdown is generally lacking, and relatively large amounts are commonly lumped together as "miscellaneous". It is even frequently impossible to distinguish between debt interest and debt retirement payments. The local government of any given area may be in the hands of several bodies—say a village council, a township council, a county council, a school board, a health board, a public utility board, etc., with different boundaries, different fiscal periods, and different systems of accounting, and to disentangle the affairs of these overlapping bodies and secure any consolidated statement of their financial operations and position is well-nigh impossible. Furthermore, what statistics are available in most of the provinces relate only to very recent years. A historical study of municipal finance in general is, therefore, almost impossible. While some of the more recent reports of the provincial departments of Municipal Affairs are more satisfactory, the need for a greater degree of co-ordination and co-operation between provincial and municipal governments with respect to municipal finance statistics remains urgent.

In spite of these serious deficiencies in the material available, and the limitations of the use which can be made of the product, the Commission has attempted to compile statistics on a comparable basis for every province, classified in a manner

--There are in Canada some 27,959 local councils and boards with a combined membership of about 125,000 persons, paid and unpaid. Ex. 267, Brief of the Citizens' Research Institute of Canada, p. 8.
complementary to the Dominion and provincial accounts. Instead of the customary classification by cities, towns, villages, and rural municipalities, which is of little value for purposes of analysis owing in part to the great variations in provincial definitions of the units, a new and more significant grouping has been employed—Metropolitan areas, other urban, and rural. "Metropolitan areas" (Montreal, Toronto, Winnipeg, Vancouver, and Windsor) consist of the major cities and their immediately surrounding and dependent towns, villages, and suburban townships. "Other urban" includes all other cities, towns, and villages, in general of more than 500 inhabitants, and "rural" all remaining municipal organizations, although the division between "other urban" and "rural" is in some cases only approximate. The selected metropolitan areas account for something more than two-fifths of all municipal revenues and expenditures, the other urban units for something less than two-fifths, and the rural units for one-fifth.

For details of the methods used by the Commission and the qualifications which should be noted before use is made of the statistics the reader is referred to the Introduction to the Municipal Section in Book III.

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3 This task would have been impossible without the able and willing assistance of Mr. Joseph Howes of the Citizens' Research Institute.

4 There are several cities—Quebec, Ottawa, Hamilton—larger than Windsor, but they have not the distinctive metropolitan characteristics and problems of Windsor. Greater Ottawa, including Hull, might be considered a metropolitan area, but this was not practical for our present purposes owing to the provincial division of the area.
2. Municipal Functions

Municipal expenditures for 1937 are summarized in the following table, and details are given for selected years in the Municipal Section of Book III.

**MUNICIPAL EXPENDITURES, 1937**

<table>
<thead>
<tr>
<th></th>
<th>Metropolitan</th>
<th>Other Urban</th>
<th>Rural</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net debt service</td>
<td>52</td>
<td>19</td>
<td>4</td>
<td>75</td>
</tr>
<tr>
<td>(Millions of Dollars)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Education (net,</td>
<td>28</td>
<td>10</td>
<td>18</td>
<td>56</td>
</tr>
<tr>
<td>after provincial</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>grants)..............</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Public Welfare,</td>
<td>28</td>
<td>15</td>
<td>7</td>
<td>53</td>
</tr>
<tr>
<td>including relief</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Streets and roads</td>
<td>7</td>
<td>11</td>
<td>13</td>
<td>31</td>
</tr>
<tr>
<td>(net, after</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>provincial grants)...</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>General Government,</td>
<td>31</td>
<td>24</td>
<td>12</td>
<td>67</td>
</tr>
<tr>
<td>and all other</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>expenditure).........</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Debt retirement</td>
<td>126</td>
<td>102</td>
<td>56</td>
<td>284</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

*Education and Public Welfare.*—These two major municipal functions have certain important characteristics in common, and for our present purposes can be conveniently discussed together. Education accounts for 33 per cent of municipal current expenditures excluding debt charges, and welfare services for 23 per cent.* It is evident that these services will bear the full impact of wide differences in taxable capacity which may exist between different municipal units, and that great differences in ability to support these services on the scale needed today will have very serious consequences.

The great variations which exist in the ability of municipalities to support these services arise in part from the failure to make the municipal unit conform to the changing economy and coincide with an economic unit; in part from the very uneven distribution of taxable income and wealth which has accompanied the development of a nationally integrated economy with a high degree of specialization; and in part from the great expansion and changed nature of the demands made on these services.

The most striking examples of the failure of the political municipal unit to conform to the local economic unit are the component municipalities of the metropolitan areas, and the rural units designed in horse and buggy days. A metropolitan area will normally contain some very wealthy residential suburbs organized as separate municipalities, and some very poor dormitory suburbs; some units that are mainly industrial; some that are commercial; and some "twilight" zones of obsolete residential property. These units may be all parts of one economic organization but there will obviously be the greatest extremes of difference in their financial ability to supply their residents with services. Property assessment per pupil, for example, sometimes differs as much as ten to one. Equally wide differences may exist between adjoining rural municipalities arbitrarily laid out and of exactly the same area, but very different in resources and other economic advantages.

Many of the differences, however, are not due merely to the failure to make political boundaries conform to the appropriate economic unit. One of the prices paid for the higher national income and standards of living achieved since Confederation has been the virtual disappearance, or great reduction in importance, of the small local economic unit. It has been absorbed in the nation-wide, and worldwide, organization of business. There is no longer any necessary or even likely relation between the wealth a municipality produces and local property values and service requirements. Yet responsibilities have been delegated to municipal governments which are justifiable only on the assumption that the local political unit will also be an economic unit with a per capita income not far removed from the provincial average.

But while the differences between taxable capacity of local political units have been increasing, as a natural corollary of the type of economic development which Canada has experienced, the relative cost of education and welfare services, and the need for approximate uniformity in the standards of services provided, have also been increasing. The complex and mechanical modern society is a machine which can produce much more wealth than the self-sufficient units of former days, but it requires a highly trained and well-informed public to run it successfully. If full advantage is to be taken of modern productive facilities, more intensive and longer periods of general education are required; more subjects must be taught; more equipment and more trained specialists are needed; and special and often extensive instruction must also be provided for the various grades of subnormal intelligence which in earlier societies it was safe to leave uneducated. There are similar increases in the need for welfare services arising from the loss of the former degree of family self-sufficiency, the abrupt fluctuations which are characteristic of our present economy, and advances in medical and related sciences. In the cases of both education and welfare, the concentration of population in the cities has made possible the provision of higher standards but has also multiplied costs.
These developments have been discussed in detail in our historical review in Book I as aspects of the evolution of the economy which are of basic significance to Canadian public finance and the federal system. We are here concerned only with noting the impact of these changes on municipal institutions, and in particular the extent to which approximate uniformity in ability to provide the basic social services has ceased to be a valid assumption.

Streets and Roads.—A significant contrast exists between the trend of development of municipal welfare and education services, and that of the other chief municipal function—the provision of streets and roads. The development of the automobile made necessary entirely new types of both urban and rural roads, on a hitherto unprecedented scale, and was an important factor in shifting population to outlying suburban areas. The municipalities were thus faced with almost immediate necessity of making a tremendous capital investment, that was bound to cause in many cases a reduction in property values through shifts in population which it would facilitate. Extensive programs for reconstruction of urban streets which were launched in the immediate pre-War years were of necessity stranded during the War, but were afterwards carried to completion in a surprisingly short period of time. By the middle twenties virtually all the urban municipalities had rebuilt their streets, and made the necessary attendant changes in sewers, sidewalks and street lighting facilities to meet the new demands. It is true that some of this investment is already obsolete owing to the continued growth in automobile traffic, and that expensive express and overhead arterial roads will have to be cut through congested areas, but the accomplishment of the urban municipalities in equipping themselves with relatively modern and complete facilities in such a short period of time remains a notable one.

It was clear from the first that a satisfactory network of rural roads could not be planned, financed, and built by the rural municipalities. As a result, provincial governments stepped in and progressively assumed an increasing proportion of the capital and upkeep expenditure, although the degree and method of participation varied widely. Possibly because the variations in road standards provided by poor and rich municipalities were more directly evident than equally important variations in welfare and education services, and because the need arose more suddenly and strikingly, and because there were pressure groups more directly interested and better organized, the logic of pooling resources in the common interest was brought home more rapidly. Urban municipalities did not benefit equally from provincial assistance, although provincial governments have in many cases assumed the expense of the costly main highway approaches to the larger centres, and there are important indirect benefits from the lower transportation charges and enlarged market afforded by the provincial highways. Nevertheless, it would appear that since the advent of the automobile, urban municipal taxpayers have borne a particularly heavy burden for the provision of modern streets and roads. The bulk of the capital borrowing for this purpose was on a ten to fifteen year basis, with relatively high and progressively increasing amortization charges, and as a result those municipalities which have been able to maintain their debt retirement schedules are now extinguishing their remaining road debts very rapidly. This factor largely explains the buoyant position of Ontario municipal finances in particular, although it may well be charged that the rapid equipment of the urban areas, and their present strong financial position, have been achieved by something in the nature of a discriminatory capital levy on real estate owners, for the taxes may not cease when the roads are paid for but may be continued for other purposes.

It has not been attempted to do more in this review than to note the effect of the changes in basic conditions on the ability of municipalities to carry out their traditional functions. These functions have grown more costly and more complex as a natural correlative of the development of the economy; the economic basis of the municipality which determines its ability to perform these functions has meanwhile grown more narrow and vulnerable; as a result the traditional administrative unit is today too small and limited to perform these functions efficiently or distribute their costs equitably. We have noted the extent to which provincial governments have recognized this fact in the provision of streets and roads, and the extent to which it has been neglected in the provision of welfare and education services.

Appropriate adjustment of municipal administrative units to modern conditions, and greater equalization of the chief municipal burdens, are, of course, entirely a matter of provincial jurisdiction and discretion. Plan I, however, by putting all provincial governments in improved and more stable financial positions, makes possible reorganization and reforms along lines which would remove important sources of some differences and inequities which threaten national unity and welfare today.

*Estimated municipal debt for streets, roads, and bridges in Ontario fell from $183 million in 1930 to $160 million in 1936, and has since declined at an even more rapid rate.*
3. MUNICIPAL REVENUES

Municipal revenues for 1937 are summarized in the following table, and details are given for selected years in Part 3 of Book III:

MUNICIPAL REVENUES, 1937

<table>
<thead>
<tr>
<th></th>
<th>Metropolitan</th>
<th>Other Urban</th>
<th>Rural</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Millions of Dollars)</td>
<td>100</td>
<td>91</td>
<td>52</td>
<td>245</td>
</tr>
<tr>
<td>Real Property Taxes</td>
<td>6</td>
<td>1</td>
<td>1</td>
<td>8</td>
</tr>
<tr>
<td>Sales and Income Taxes</td>
<td>8</td>
<td>11</td>
<td>1</td>
<td>20</td>
</tr>
<tr>
<td>Other Taxes (*)</td>
<td>5</td>
<td>4</td>
<td>1</td>
<td>10</td>
</tr>
<tr>
<td>Licences, Permits, Fees</td>
<td>2</td>
<td>4</td>
<td>1</td>
<td>6</td>
</tr>
<tr>
<td>Public Utility Contributions</td>
<td>10</td>
<td>6</td>
<td>5</td>
<td>21</td>
</tr>
<tr>
<td>Other Current Revenue (*)</td>
<td>133</td>
<td>116</td>
<td>59</td>
<td>308</td>
</tr>
<tr>
<td>Provincial Government Grants</td>
<td>4</td>
<td>0</td>
<td>0</td>
<td>4</td>
</tr>
</tbody>
</table>

(*) Chiefly business taxes, and also (in the Maritimes) personal property taxes.
(1) Rentals from municipal property, interest and penalties on tax arrears, and miscellaneous income of all kinds, some of which should probably be credited to capital account.
(2) Not included in revenue totals but deducted from appropriate expenditures in the table on p. 142.

Of the total, which was 31 per cent of the revenues of all governments in Canada in 1937, 80 per cent is derived from real property taxation. The real property tax is at once the largest single tax in Canada and, for the reasons briefly discussed in the foregoing sections, one that is called on to meet functions the cost of which varies tremendously between local units of government. As a result we find many instances in which this tax (which for the bulk of the population is the heaviest paid in the course of the year) is twice as much in relation to property income for residents of some areas as for those other areas in the same province. There are extreme instances in which this tax (which for the bulk of the population is the heaviest paid in the course of the year) is twice as much in relation to property income for residents of some areas as for those other areas in the same province. There are extreme instances in which this tax (which for the bulk of the population is the heaviest paid in the course of the year) is twice as much in relation to property income for residents of some areas as for those other areas in the same province.

Examples are numerous and well-known, and many were given in evidence before the Commission, where the tax amounted to practical confiscation, or to a forced and inequitable capital levy, and where it forced the abandonment or destruction of property. More difficult to establish and illustrate, but perhaps of even greater general importance, is the effect of the pressure of the tax on individuals and business enterprises in marginal positions throughout Canada, and particularly in depressed areas.

Taxation of Real Estate

It is very generally maintained that property taxation as a whole is too high. This general proposition is based sometimes on one, sometimes on another set of circumstances. People have, for instance, been ejected from their homes because they were unable to pay the taxes. Here the proposition would mean either that incomes are too low or alternatively that, where low incomes prevail, it is wrong to impose a tax on a necessity of life such as shelter. Others have found that property which has ceased to yield an appreciable income is still subjected to heavy taxation. This situation has led to the surrender of property to the taxing authority and in other cases to the demolition of buildings which cannot command rents in keeping with their assessments. In this case it may be rather the method of assessment than the property tax itself which is at fault. Others complain that the income from real property is more heavily taxed than income from other investments. In one sense this is true, but it must be remembered that a property tax, once imposed, tends to be capitalized so that the value of the property is reduced once for all by the capitalized value of the tax, just as it would have been reduced had it been subjected to a mortgage of equal amount. Any subsequent purchaser pays the reduced price and presumably gets the same net return on his investment as if he made alternative investments. The initial act of confiscation may be deplored. It cannot be redressed years later without the unjustifiable enrichment of subsequent purchasers of the property.

(1) The following briefs complain of unduly burdensome or inequitable taxation of real estate:
Ex. 7, Brief of Manitoba, Pt. VII; Ex. 8, Brief of Manitoba, Pt. VIII; Ex. 9, Winnipeg Real Estate Board; Ex. 17, Winnipeg Board of Trade; Ex. 19, The Union of Manitoba Municipalities; Ex. 21, Rural Municipality of St. James, Manitoba; Ex. 24, School District of Winnipeg, No. 1; Ex. 25, Manitoba School Trustees’ Association; Ex. 28, The Greater Winnipeg Youth Council; Ex. 31, The Home and Property Owners Association of Winnipeg; Ex. 34, Brief of Saskatchewan; Ex. 49, Saskatchewan Urban Municipalities Association; Ex. 90, Regina Board of Trade; Ex. 97, Saskatoon Board of Trade; Ex. 98, Ontario Association of Real Estate Boards; Ex. 113, Canadian Federation of Mayors and Municipalities; Ex. 172, Brief of British Columbia; Ex. 181, Municipalities of British Columbia; Ex. 182, City of Vancouver; Ex. 183, British Columbia School Trustees’ Association; Ex. 199, Vancouver Real Estate Exchange; Ex. 206, Provincial Council of Women, British Columbia; Ex. 207, Edmonton Chamber of Commerce; Ex. 283, City of Edmonton; Ex. 284, City of Toronto; Ex. 285, The City of Toronto and Ontario Mayors’ Association; Ex. 288, Property Owners’ Association of Toronto; Ex. 301, East York Business Men’s Association; Ex. 308, Home Builders’ Association of Toronto; Ex. 307, Brief of the Canadian Chamber of Commerce; Ex. 400, The Roman Catholic Separate School Trustees’ Association of Ontario. See per contra Ex. 105, Brief of the Single Tax Association of Canada.
In still another sense taxation on real property may be said to be too high. A municipality to function adequately requires a certain revenue. It may be impracticable to obtain this revenue by taxing land and improvements if a point is reached at which an increase in the rate of the tax would not produce an increase in its yield. Or it might be highly unjust to continue to tax land because in so doing revenue would be raised by imposing an undue burden on one group in the community while imposing no proportionate burden on other groups. The fact, already noticed, that the real property tax tends to be capitalized is a matter of aggravation in respect of this inequity whenever what is under consideration is not the continuance of high rates of long-standing but a further increase in the rates. Many large municipalities which press for financial relief fully realize that if this relief were extended to all municipalities any tax by which it was financed (whether Dominion or provincial) would take more from their citizens than the municipality itself would receive. Here the essence of the complaint is that the municipality has been required to finance costly services without being given adequate powers of taxation. The remedy would lie either in decreasing the demands made on the municipality or in supplementing its revenue by some form of provincial grants-in-aid. For these various reasons the cry arises on all sides that the taxation of real property is too high, but this is an opinion which cannot in most cases be proved or disproved by any objectively determined scientific criteria.

It is argued that the failure of the construction industry to make any substantial recovery is evidence that real property taxation as a whole is excessive, and that a reduction in rates would divert the marginal consumer's dollar into better housing instead of into alternative, and possibly less socially useful, channels. And it is charged that a tax of such a rigid nature as the Canadian real property tax is particularly unsuited for a country such as Canada, already burdened by a high fixed overhead which has to be supported by a sharply fluctuating income, and that the heavier the tax, the more vicious and undesirable its effects. Unquestionably in many areas the tax was established at a high rate during a period of rapidly rising land values, and was deliberately intended to contain some element of the "single" tax, or of a capital gains tax; the justification for this naturally disappears once the trend of land values flattens out or drops sharply.

The Commission believes that there is great weight in these general contentions even when they cannot be statistically established, or related to other than hypothetical alternatives. In this connection the benefit to municipalities of the Commission's recommendations in Plan I should be noted. On the 1937 base they would provide a net saving to municipalities of some $20 million, or 8 per cent of the real property tax. This saving, of course, would not be evenly spread, but largely concentrated in the chief distressed areas.

But although no positive finding can be made on the abstract contention that real property taxes are too high, particularly in the absence of proposals for compensatory alternatives, certain gross inequities which now exist can be specifically noted. They are, chiefly, different levels of taxation (to support the same functions) in different municipalities; and great variations in taxation, as a percentage of income, even in the same municipality.

The different levels of taxation in different municipalities arise from the performance of similar functions with very different means. The remedy, as has been suggested in the previous section, is the reorganization of municipal units more in conformity with modern economic conditions. In addition certain services might be pooled (whether through the provincial government or among a group of municipalities) so as to redistribute the cost of services in relation to capacity to pay.

The variations in taxation, as a percentage of income, between individuals in the same municipality result from the assessment of taxation on an assumed capital value of real property rather than on income. Although the assessed capitalization is supposed to be closely related to, or specifically based on, earning power, it is in many cases not so in fact owing to faulty assessments, unrecognized changes in earning power, or inability to rent a property at all. The first of these defects may be due to lack of competent assessors; the second, to lack of sufficiently frequent re-assessments and facilities for appeal; the third is inherent in the present system of taxation. To correct the inequity of taxing an individual on the capitalized value of an income which he cannot make would not require as drastic a change as putting all property taxation on an income basis. (Even in the countries frequently cited as examples of a more equitable system of property taxation on an income basis there is a large element of arbitrary valuation.)
It would appear that a rough adjustment of this particular inequity could be achieved if allowance were made for a rebate of a portion of the tax applying to improvements (although not to the land) when it was established that it had not been possible to rent the property on reasonable terms during, say, six or nine months of the year.* The property should in any case be taxed sufficiently to cover the cost of services rendered to it. To the contention that such a provision would reduce the stability of municipal revenues it could be replied that under conditions in which the operation of such a provision would be of any importance, the revenues under the present system are only superficially stable, bolstered up by uncollectable tax arrears,† and that it is grossly unfair virtually to confiscate the property of those who have already been the chief sufferers from adverse rental conditions.

**Tax Exempt Crown Property**

It was also complained to the Commission‡ that it was unjust to exempt Crown property from taxation when that property was being used for some normal commercial purpose, such as electric power distribution, and would, if in private hands, be taxable; or when it was being used in a profit-making commercial enterprise, such as a provincial liquor store. The Commission suggests that such

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* The Ontario Assessment Act, c. 272, s. 125, makes a certain vacancy allowance on property which is not rented.
† Municipal tax arrears rose $78 million between 1930 and 1935.
‡ Ex. 50, Sask. Assn., Rural Municipalities; Ex. 109, Can. Electrical Assn.; Ex. 150, Union of N.S. Municipalities; Ex. 158, City of Halifax; Ex. 159, Halifax Board of Trade; Ex. 181, Municipalities of B.C.; Ex. 207, Citizens’ Research Institute; Ex. 281, Ont. Municipal Assn.; Ex. 255, Toronto Property Owners Assn.; Ex. 343, Chambre de Commerce de Montreal; Ex. 394, Can. Chamber of Commerce.

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property should be subject to taxation on the same terms as that of private enterprises.

A somewhat different problem is presented by Crown property which is not being used for any commercial purpose, but which involves the municipality in considerable expense.* This is especially the case with respect to military property. On the other hand, the municipality frequently benefits substantially from the presence of the Crown property such as post offices and legislative buildings. The Commission can make recommendations only in very general terms. The Commission recommends that the senior governments should make payments *ex gratia* in place of taxation in respect of all property (other than commercial enterprises which should be assessed and taxed on the same basis as private property) held by them in municipalities, but that the amount of these payments should depend on the nature of the property and the extent to which it benefits from municipal services. It may even be expedient for both senior governments to lay down some general principles to govern these payments and to employ arbitrators to apply them to individual properties in the event of being unable to reach an agreement with the municipality. The principle is clear that the burden of providing services for government properties should be spread widely by federal or provincial taxation, as the case may be, and not charged against neighbouring properties. But the amount of the payment appropriate in each case will depend on a number of circumstances, of which the assessable value of the property may not be one.

* E.g., Halifax and Esquimalt. It was declared in evidence to the Commission (p. 2398) that in the latter city out of $9,700,000 for improvements, $8,212,000 was tax-exempt.
4. MUNICIPAL DEBTS

Municipal debts are on the whole more closely related to municipal capacity to bear them than are the chief municipal functions. A poor municipality may incur just as great costs per capita as (or even larger costs than) a rich one in providing education, for example, but it is extremely unlikely to have as heavy debt charges, simply because it could not in the past have borrowed as much money. On the other hand, it is true that a poor municipality may have to forgo desirable capital works and improvements because of its poor credit standing.

In general, municipal indebtedness is closely related to the corresponding asset, and, ideally, is amortized within the life of the asset. But wide latitude is frequently given to estimates of the life of the assets. In recent years particularly, the funding of general deficits (largely caused by relief expenditures) has obscured this relation somewhat, but the contrast with the general debt of the senior governments remains notable. (It is interesting to note that most provinces originally also earmarked their borrowings for specific purposes, and undertook to amortize them accordingly, but as time went on, and as through refundings and funding of general deficits the debts became increasingly confused and indistinguishable, even nominal adherence to this practice was discarded.) Outstanding municipal debt in 1937 may be classed roughly as follows:

**MUNICIPAL DEBTS, 1937**

<table>
<thead>
<tr>
<th></th>
<th>Metropolitan</th>
<th>Other Urban</th>
<th>Rural</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Millions of Dollars)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Schools</td>
<td>115</td>
<td>87</td>
<td>15</td>
<td>317</td>
</tr>
<tr>
<td>Roads, streets and bridges</td>
<td>199</td>
<td>139</td>
<td>27</td>
<td>365</td>
</tr>
<tr>
<td>Other general</td>
<td>317</td>
<td>144</td>
<td>12</td>
<td>473</td>
</tr>
<tr>
<td>Gross general</td>
<td>681</td>
<td>381</td>
<td>64</td>
<td>1,086</td>
</tr>
<tr>
<td>Less sinking funds</td>
<td>106</td>
<td>71</td>
<td>8</td>
<td>182</td>
</tr>
<tr>
<td>Net general</td>
<td>615</td>
<td>209</td>
<td>49</td>
<td>854</td>
</tr>
<tr>
<td>Utility—net</td>
<td>143</td>
<td>99</td>
<td>15</td>
<td>257</td>
</tr>
<tr>
<td>Guaranteed—net</td>
<td>45</td>
<td>2</td>
<td>—</td>
<td>45</td>
</tr>
<tr>
<td>Bank loans</td>
<td>52</td>
<td>36</td>
<td>24</td>
<td>112</td>
</tr>
<tr>
<td>Total, net</td>
<td>755</td>
<td>426</td>
<td>88</td>
<td>1,269</td>
</tr>
</tbody>
</table>

With a few notable exceptions municipal debts, in contrast with Dominion and provincial debts, have not increased since 1930. Severe retrenchment has been necessary in a number of cases, and although relief costs have been a heavy burden for some centres, five-sixths of the total cost has been met by senior governments. The cities with a considerable increase in debt since 1930 are those in which unemployment has been concentrated, and where the cost of even 20 to 30 per cent of total relief expenditures threw municipal budgets badly out of balance. Even in these cases, however, there have been some reductions in net debt since 1934, particularly in Ontario.

On the other hand, debt charges have increased somewhat for nearly all urban areas and notably those with large relief borrowings. This is largely due to increased amortization charges on relief and deficit financing. Interest charges, as distinct from total debt charges, have tended to decline, since municipalities in a strong financial position have been able to refund on favourable terms, and municipalities in a weak position have had to reduce their borrowings rigorously. Admittedly, such a reduction may be a very undesirable one, if it enforces curtailment of socially necessary or desirable expenditures, simply because an obsolete division of municipal units throws crushing responsibilities on some areas unsuited to bear them. On the other hand, it may be a healthy check to extravagance or to optimism which the events of the depression have shown to be excessive. But there is marked iniquity in a system which imposes the highest borrowing costs, and rigid restriction of borrowing, or even total prohibition, on the haphazardly delimited local areas which are normally the poorest, or have been the hardest hit, as a result of cyclical developments and national policies beyond their control.

The hardest hit municipalities were forced into default, and it is illuminating to analyse the factors responsible for these extreme examples of breakdown. These examples may properly be called extreme since the effort made by most Canadian municipalities to honour their obligations, at the expense of drastic reduction in desirable services, is striking. Generally speaking, defaults occurred only under intolerable strain and pressure. Roughly classified, defaults occurred in*:—

(a) working-class dormitory suburbs—i.e., the poorer residential districts—of metropolitan areas;

(b) one-industry towns, in which the one industry was closed down by the depression;

(c) rural, and dependent urban, units where the whole area had been overwhelmed by natural disaster, such as the Western drought.

* Defaults by derelict towns resulting from miscalculation as to the economic future have, of course, occurred in many regions throughout Canadian history.
Examples in the first class are but further evidence of the chaotic condition of municipal organization in Canadian metropolitan areas. Large blocks of poorer class residential areas which were arbitrarily segregated into separate municipalities, whose inhabitants were particularly hard hit by the depression, and whose local relief and welfare services increased correspondingly, were inevitably saddled with an inequitable and frequently overwhelming share of depression burdens. At the same time neighbouring municipalities, which were part of the same economic unit but which harboured a more fortunate or sheltered group, had no increased responsibilities to face, and were able to take advantage of depression conditions to reduce costs and cultivate a smugly superior attitude to their less fortunate neighbours. The other classifications, which taken together account for only a small portion of the defaults, are simply among the minor routine casualties of modern hit-and-run society, but even in their cases organization of the local administrative units more in conformity with modern economic conditions, and more even spreading of the risks, would have reduced the casualties.

Consideration of municipal defaults must include the constitutional questions of whether provinces, by virtue of their exclusive power to legislate concerning municipalities, may legislate with respect to insolvent municipalities and of whether they may deal with the bonded indebtedness of a municipality which is not insolvent. Whatever the answers, it is obvious that a province could, by valid legislation, make it difficult or impossible for the creditors of a municipality, whether solvent or insolvent, to collect their debts. Nor would it have any difficulty in turning a solvent municipality into an insolvent municipality if this were a necessary condition for securing jurisdiction over its affairs. The Commission thinks that in such matters the jurisdiction should be clear and the responsibilities precise, and it recommends that if the British North America Act is amended, provinces should be given specific power to legislate in respect to municipal debt whether or not the municipality concerned is solvent.

In this respect the Province of Quebec stands in a special position. If Plan I is implemented, the Dominion will have to assume a portion of the municipal debt of that Province. The distribution of the benefits to the municipalities would, of course, be within the discretion of the Province, but presumably it would wish to deal with the debt situation in the metropolitan area of Montreal. This might require legislation dealing with the debt of municipal units of very different credit standing, and it would be essential that the Province should have adequate legislative power to deal with the situation effectively.

**Provincial Supervision of Municipal Borrowing**

The degree of provincial responsibility for the conduct of a municipality's affairs is variously interpreted. But it would seem clear that when the provincial government creates a subsidiary body, and delegates to it certain revenue powers and responsibilities, it should see to it not only that these powers are adequate, with efficient management, to match the responsibilities, but also that there is efficient management. This obligation would appear to be particularly important for individuals who loan money to the municipality on the obvious assumption that the provincial government will not establish conditions, or permit conditions to develop, which may make its repayment impossible. Indeed, there is an even stronger case for a province to stand behind the credit of the local government bodies which it has created than for the Dominion to stand behind the credit of the provinces as has been recommended in Plan I. In addition to providing for an approximate matching of revenues and responsibilities (and, as suggested in the previous sections, a substantial measure of pooling of resources and averaging of expenditures to remove the wide existing differentials) the province should supervise adequately municipal borrowing. Supervision of borrowing would ideally include not only an examination of the purpose and immediate need for the borrowing, but also determination of the best form and terms of the borrowing, and continuing regulation of sinking funds, or repayment, provisions. Some or all of these forms of control are now exercised, although with widely varying degrees of strictness, by each province. If a municipality's borrowings are excessive it may be because the province has saddled it with greater responsibilities than revenue powers, or because the municipality's affairs are being incompetently handled, or because the municipality's growth has been checked by unfavourable, and possibly unforeseeable, circumstances. In any case the province has a responsibility, both to creditors and prospective creditors of the municipality, and to taxpayers and recipients of services in the municipality. This responsibility can be exercised to some extent by close supervision of municipal borrowing, and of municipal budgeting, accounting, and administrative practices; perhaps even more importantly, by providing conditions under which a municipal civil service—adequately paid, professionally trained, and politically independent—can develop.
If provincial governments supervise municipal borrowing closely and enforce efficient administrative practices, municipal credit should quickly reflect the increased measure of security. Indeed, under these conditions (and assuming an equitable division of revenue powers and expenditure responsibilities) the credit of a municipality should be as good as that of a province. In addition, municipalities, as a result of their practice of earmarking their borrowings and relating their debts to specific assets, normally pursue conservative debt retirement programs—always an attraction for the investor. However, there may be circumstances under which a province will wish to assume municipal indebtedness, either by refunding debts or by guaranteeing them. It may, for instance, feel that its municipalities are not receiving the credit rating to which they are entitled; or that some of them have been unduly burdened in the past by obligations which the province itself would have met if it had had the means to do so; or that certain municipal amalgamations are desirable and that an advantageous debt settlement is a necessary preliminary. In such cases a province would, if Plan I were implemented, have two courses open to it. It might employ the sole credit of the province, in which case it could not count the obligations which it assumed in making an estimate of its fiscal need when seeking an enlargement of its National Adjustment Grant; or it might endeavour to carry out the refunding through the machinery recommended under Plan I. In the latter case the debt would have to be approved by the appropriate body which (as has been explained in an earlier chapter) would consider all the circumstances, including the credit of the Federal Government and its ability to guarantee the debt. If approved the debt would become an obligation of the central debt agency, but the municipality or municipalities concerned would have undertaken to reimburse the agency for the debt charges and would, presumably, have been required to assign revenues for this purpose. In addition the province would have underwritten the debt. If refunding of this character were resorted to, it would lie with the province to decide whether the heroic debt retirement provisions which appeal to private investors should be adopted or whether they should be modified so that the municipality, with its debt charges substantially reduced, might be in a position to finance future capital expenditures on a pay-as-you-go basis with economy to its taxpayers.

IN CONCLUSION

Local and municipal institutions fall under the exclusive jurisdiction of the province, and the Commission has, therefore, refrained from making specific recommendations with respect to municipal reform, except where the problem falls within Dominion-provincial relations. The Commission has sought rather to outline the problems which must be faced, assuming that municipal reform will sooner or later be undertaken by the provinces. It should be noted that, if the Dominion assumes responsibility for unemployed employables and if the Commission's financial recommendations are implemented, not only will the municipalities derive direct benefits, but the provinces will be in a much better financial position to attack the problem of municipal reform than heretofore.

The Chapter discusses some of the more fundamental problems which must be faced if municipal financing is to be efficient and municipal taxpayers are to be equitably served. It has pointed out that the size of the municipal unit in metropolitan and rural areas is, in very many cases, no longer economic or in keeping with administrative efficiency; that local needs no longer determine municipal functions and that many functions, essentially provincial, are still left with, or have been imposed on, the municipalities; that municipal revenues are in many cases far from adequate to support municipal functions; that there is almost universal complaint across Canada of undue, or inequitable, taxation of real estate, though the complaints are not always well founded; that although the total of municipal debt has not risen substantially during the depression, the credit of many "one-industry" municipalities, working-class "dormitory suburbs" of metropolitan areas, and metropolitan communities generally, has been severely strained, and even destroyed in some cases, because of relief costs. The need for the provinces assuming greater responsibility for the credit position of their municipalities has also been pointed out.

The Commission has deemed it appropriate to discuss the municipal situation at some length because municipal governments were at great pains to bring their case before the Commission, which was greatly impressed with the earnest and public-spirited endeavour devoted to this basically important sphere of Canadian public life. Democracy begins with local government, and local government cannot be politically healthy and stimulating unless the problems set to those who conduct it are possible of solution. The essence of financial responsibility lies in the possibility of balanced budgets which permit of far-sighted planning, and this condition has been in grave peril in Canadian municipalities during the last decade.