

# Case-in-point

## Taking the Pulse of Planning Practice – At the Cutting Edge

An MPPI-UMCP Collaborative Initiative



### Reassessing Taxes: Tax Shifting as a Planning Tool

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### Synopsis

In planning practice, planners must solve problems with a variety of different tools. This MPPI-UMCP collaborative initiative highlights a fiscal tool: tax shifting. Tax shifting has two major functions. The first relates to municipal revenues. A major benefit to tax shifting is it allows for the diversification of revenues to meet increasing service and infrastructure demands. The second function relates to altering financial incentives and thus the behaviour of taxpayers to achieve policy goals. Tax shifting is a value-laden process which should be conducted using community derived principles. This case-in-point uses two examples, land value taxation and garbage fees, to demonstrate how tax shifting assists in reaching planning policy goals.

### Background and Introduction

Cities all over Canada are facing challenges such as sprawl, aging infrastructure, and limited revenues. These challenges are forcing planners to think outside the box and find innovative solutions. One such solution can be found in the notion of tax shifting. Tax shifting is a financial lever that planners can use to achieve policy goals such as encouraging compact form, addressing environmental problems, and revitalizing older neighbourhoods.

This case in point highlights the merits of tax shifting as an innovative planning tool. While taxation has traditionally been recognized as a means to raise revenue for the services and infrastructure that governments provide, it can also be used as a tool to shape economic growth and development which influences the morphologies of cities and communities. This collaborative initiative examines how tax shifting, used in tandem with other tools, can help meet long term policy objectives. In particular, two types of tax shifting are examined: land value taxation and user pay garbage fees.

**Explanation of Tax Shifting as a policy tool from the Centre for Integral Economics**  
 “In its role as a tool of governance, the tax code can be likened to the genetic code of an organism, sending out signals that influence a multiplicity of economic decisions thereby directing patterns of investment and development. Unlike regulatory mechanisms or public education, tax policy exerts a constant, dynamic influence on private and corporate decisions and, thereby, on development patterns.”  
<http://www.integraleconomics.org>

**How does tax shifting work?**

Everyday each Winnipegger makes numerous individual decisions that, when aggregated, have serious planning implications. For example, the decision to recycle results in waste minimization which in turn is directly related to the lifespan of landfills, collection and disposal methods, and civic revenue and expenditures. There are many ways a municipality can choose to influence these decisions. Command and control methods such as fines or penalties can be effective, if somewhat heavy-handed. At the other end of the spectrum moral arguments, as expressed in the need to preserve resources for future generations, can encourage individuals to compost, recycle, or reduce consumption. Tax shifting offers an alternative strategy. It represents a financial lever that is a reinforcing and consistent reminder that

discourages ‘undesirable’ behaviour by increasing its price, in this example, by introducing a fee for garbage disposal. It is based on the simple premise that if something increases in cost, individual choice will be affected: people will participate less in that activity or reduce their consumption of that good.

While tax shifting has the potential to increase, decrease, or hold constant the total revenues collected by a municipal government its greatest benefit may be in its ability to diversify municipal revenues (see figure 1). Currently, the City of Winnipeg like many municipalities across the country is over-reliant on property taxes. This is problematic in that there is little natural growth to property tax as a stream of revenue; it must be constantly raised to meet funding demands. This is not the case for income and sales taxes which grow naturally with the economy. Also, the scope of municipal services has expanded in areas that cannot be described as services to property (recreation and library services, for example) and should not, therefore, be funded through property taxes.

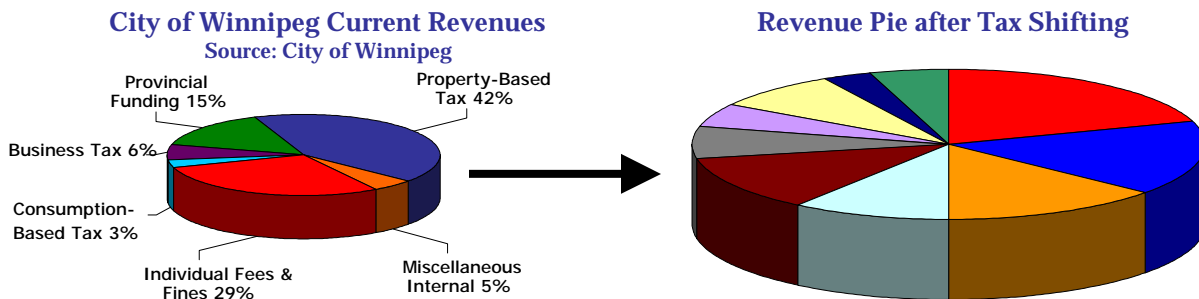


Figure 1: The pie chart on the left displays current revenue sources for the City of Winnipeg. The pie chart on the right represents a tax shift that results in greater and more diversified revenues.

Tax shifting can affect the pocketbooks of taxpayers in a variety of ways as well. Due to the nature of tax shifting, even if the tax shift is revenue neutral to the municipality, some residents may pay more tax and some may pay less tax. For this reason tax shifting is almost always controversial. However, tax shifting can give residents flexibility in the amount of taxes they pay, especially if the tax shift involves user fees.

## A Principled Approach to Tax Shifting

**T**ax shifting is a value-laden exercise. When choosing between alternative forms of taxation, the litmus test ought to be the merits of that form of taxation in relation to a set of principles recognized as important by the broad community. These might include:

- § Equity – meaning that the tax is fair; that it considers ability to pay while recognizing that those who benefit from a service ought to help fund it
- § Economy – meaning that the tax system promotes a prosperous economy which benefits all citizens
- § Environment – meaning that the tax instruments encourage behaviours that protect the natural environment
- § Ease of administration – meaning that the revenue source is easy to administer and collect
- § Efficiency – meaning that the tax collected represents the most efficient use of resources
- § Accountability – meaning that the government should be held accountable for both the level of service and the revenue they collect to fund the service
- § Transparency – meaning that there is an association between the taxes people pay and the service they receive
- § Harmony – meaning that the tax instruments support the municipality's long-range goals and create the kind of community that citizens want
- § Reliability – meaning that the municipality can count on the source of revenue over time
- § Diversification – meaning that the municipality should not depend too heavily on one revenue source

## Tax Shifting in Practice

**W**hat follows are two examples of tax shifting. The first examines the concept of Land Value Taxation (LVT) as an alternative to property taxation as currently applied in most municipalities. The second example looks at the introduction of a user fee for garbage service.

### Property Taxes vs Land Value Taxes

Property taxes are taxes on two different assets. Land is taxed as well as the buildings sitting on the land. Taxes are paid on the assessed value of both assets combined.

Studies have shown that on average in North America, land makes up 30% of the assessed value and the buildings make up 70% of the value.<sup>1</sup> Land values are socially determined by a variety of factors the most important being the social capital and investment surrounding that piece of land. For example, a vacant lot serviceable with sewer, water and electricity and close to social infrastructure such as schools, hospitals, and recreation centres is worth more than an identical lot on unserviced agricultural land. The buildings are assessed as to their condition and or how much revenue they generate in the case of business taxes.



Shifting taxes from buildings towards land discourages parking lots like this one on Assiniboine Ave in Downtown Winnipeg.

Socially determined land values combined with a property tax system that taxes the building on the land have negative planning implications. In Downtown Winnipeg there are many vacant lots used as parking lots even though they can be easily fully serviced and are in a central location. The revenue generated from the parking lot allows the owner to cover the cost of property taxes while ‘sitting’ on the property for years waiting for social investments to increase the socially determined value of the land. The lots are then sold for a profit called economic rent. A tax on the land value rather than the building will capture economic rent. By increasing the cost of holding land, land value taxation reduces speculation as well as encourages the development of vacant lots. The results of this tax shift support the objective of a vibrant downtown.

Property taxes have several effects on the morphologies of our cities. Due to the fact that 70% of the assessed value comes from the building and not the land there is a disincentive to make improvements to buildings and the housing stock. By shifting taxes away from the buildings and onto the land it encourages different behaviours. Underused buildings and/or housing are now cheaper to upgrade which encourages policy goals such as compact form and increased densities. Further, this satisfies the principles of sustainability and thoughtful development.

### Garbage Fees

Garbage fees are an excellent example of tax shifting. Currently, refuse collection in Winnipeg is funded out of general revenues. Under the City of Winnipeg’s new proposal, user fees would be introduced to pay for the service and property taxes would be reduced a corresponding amount. This tax shifting is revenue neutral but it is hoped it will change taxpayer’s behaviour in a manner that supports policy objectives in Plan Winnipeg.

<sup>1</sup> Centre for Integral Economics, October 2003. Land Value Taxation: Issues and Directions for the City of Winnipeg, p.20

Many municipalities across North America have begun to reap the benefits of garbage fees. By placing a cost on disposing of waste there is an incentive to reduce waste. If recycling (a 'good') has no cost and each bag of garbage (a 'bad') has a cost, there is an incentive to change behaviour and increase the amount of recycling or composting. Further, consumers may start demanding recyclable packaging or reduced packaging from manufacturers to further reduce their garbage costs.

The municipal government, the environment, and taxpayers receive the benefits of garbage fees. The municipality delays capital expenditures on new landfills and recycling creates a revenue stream that offsets the costs of a recycling program. The environment benefits from fewer landfills and reduced consumption of raw materials due to the increase in recycling and reduction of waste. Taxpayers benefit because garbage fees are a fairer form of taxation as people who produce less waste would pay less. The transparency of government is also increased because residents can see the direct relationship between the cost of the service, the amount they pay, and the service they receive.

### Conclusion

**T**ax shifting is a fiscal tool with the ability to provide a sustained incentive to influence human behaviour in a way that supports planning policy objectives. This Case in Point highlighted two of many ways taxes can be shifted but it can be applied in a multitude of areas to support environmental, physical and social objectives. However, tax shifting is not the magic bullet to all of our planning challenges. Used in conjunction with traditional planning tools like zoning by-laws and economic development tools such as community development corporations, tax shifting is a very powerful cutting edge tool that should be added to every planner's toolbox.

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## References and Resources

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