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**CUSTOM REPORT**

# **Reinventing the West:**

## **Sustainable public policies and fiscal regimes for the 21<sup>st</sup> century**

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## Reinventing the West: Sustainable public policies and fiscal regimes for the 21<sup>st</sup> century

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## Executive Summary

### At a Glance

- Urban areas<sup>1</sup> account for a large and growing share of Saskatchewan's population, output, and employment.
- But Saskatchewan's municipal-provincial fiscal framework tends to favour rural areas over urban ones.
- As such, urban municipalities do not appear to be fiscally equipped to face the challenges of modern economic and demographic trends in Saskatchewan.
- In contrast, rural municipalities appear to have the tools to address their most pressing fiscal issues.
- This report recommends empowering urban municipalities with greater fiscal tools and increasing their share of municipal revenue sharing (MRS) funding.

This report explores the extent to which urban and rural municipalities in Saskatchewan possess the necessary fiscal tools to support economic growth and prosperity and to tackle the pressures they are facing in Saskatchewan's changing economic landscape. The report attempts to answer the following questions: Do urban municipalities have the fiscal capacity to foster sustainable growth? Will they be able to attract and retain business investment and people? Do rural municipalities have the fiscal capacity to help maintain and expand the transportation network? In other words, has Saskatchewan gone far enough to realign its suite of public policies to succeed in the 21<sup>st</sup> century economy?

To answer these questions, we first examine current demographic and economic trends in Saskatchewan. We find that the province has undergone significant changes over the past number of decades. Although agriculture will remain important to the provincial economy over the long term, strong productivity growth has reduced the need for farm workers and has pushed people to move away from rural parts of the province. A similar story is unfolding in Saskatchewan's mining industry, another rural-oriented sector. Mining represents a significant portion of the province's economic output, and an even larger share of merchandise exports, and it will likely continue to do so. But it is a very capital intensive industry, and growing more so by the day. As such, it accounts for a small share of Saskatchewan's total employment.

Both of these trends point to the growing role of urban areas in driving economic growth. Indeed, the migration of people from rural areas to urban areas is the defining characteristic of urbanization, a process that has occurred or is occurring in most of the world, including in Saskatchewan. The urban share of Saskatchewan's economic activity has been increasing alongside their share of the province's population. Indeed, cities, villages, and towns now account for the lion's share of output, population, and employment in Saskatchewan. True, a portion of economic activity in urban areas is directly and indirectly tied to mining and agriculture, but resource extraction requires highly-skilled workers in such fields as

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<sup>1</sup> This report includes cities, towns, villages, and resort villages when mentioning urban areas or urban municipalities.

engineering and geology, and most of these workers live and work in urban centres. Head office functions and other related services sector activity of these resource extraction firms also tend to take place in urban areas.

However, the strong growth of urban areas has increased pressure on municipal infrastructure and services spending, which, in turn, has strained local budgets. These pressures make it more difficult for urban municipalities to attract and retain business investment and people, both crucial ingredients for success in a hyper-competitive global economy.

On the other hand, many rural municipalities are struggling with the opposite problem: weak population growth and, in some circumstances, even declining population. This makes it difficult for these municipalities to generate sufficient revenue to help fund the maintenance and expansion of Saskatchewan's transportation infrastructure, which is crucial to getting the province's goods to domestic and international markets.

Given this context, we examine three segments of Saskatchewan's provincial-municipal fiscal framework—tax exemptions, property taxes, and municipal revenue sharing—to assess whether they are in line with the current economic and demographic realities of the province. We find that although tax exemptions are not generally geographically-driven, some are clearly geared towards sectors with strong ties to rural or urban areas. Of this subgroup, a large portion of the tax exemptions granted to the agricultural industry are not specifically aimed at achieving fairness, curb behaviours, or attain an economic objective other than reducing the fiscal burden of a specific group of individuals. A prime example is the farm fuel tax exemption. But at the same time, we also ask if tax exemptions aimed directly at the urban-oriented manufacturing industry should be replaced with a more general measure that benefits all industries equally.

Subsequently, we find that even though municipalities have tools to shift the burden of property tax across property classes —agricultural, residential, commercial and industrial—the provincial elements in the calculation of property taxes, namely the provincial percentages of value (the percentage of the assessed value of a property that is taxed) and the education mill rates, favor rural dwellings and properties. Indeed, agricultural properties have the lowest percentages of value and mill rates among all property classes. It can be argued that agricultural land owners must assume property taxes on their dwellings and their land, and thus, lower percentages of value and mill rates are warranted. However, residents of rural municipalities can reduce all or a portion of their taxable assessment on their principal dwelling by writing off the total taxable assessment of their agricultural land, leaving these residents with little or no property tax due on their dwellings.

As for municipal revenue sharing (MRS), we find that urban municipalities receive a much smaller per capita share than their rural counterparts. Indeed, rural municipalities receive more than double the funding that urban municipalities do in per capita terms. We find that the share of MRS received by rural and urban municipalities has not significantly changed since the inception of the current formula in 2011-12, although the pie is now considerably larger. When looking at economic weight, we find that Regina and Saskatoon alone account for more than half of Saskatchewan's GDP, but receive 1/3 of the MRS pie.

Overall, this report finds that rural governments appear to have the necessary support from the provincial government to keep up with their most pressing issues, but the same claim cannot be made about Saskatchewan's urban governments. The current provincial-municipal fiscal framework in Saskatchewan favours rural municipalities over urban ones. Thus, this report makes two recommendations:

- 1) Empower urban municipalities with greater fiscal tools; and
- 2) Increase urban municipalities' share of MRS funding.

Unfortunately, these recommendations come at a time when the provincial government faces a difficult fiscal situation, which has prompted it to consider significant policy reforms. We would argue, however, that whatever reforms are chosen, they should be done in the context of Saskatchewan's changing economic and demographic structure. The reforms should also be in full alignment with the Saskatchewan Plan for Growth; i.e., they should help the province's economy to better adapt and prepare for challenges as well as to promote opportunities for growth and diversification. We believe that this report's recommendations meet these criteria.

## 1. Introduction

### Chapter Summary

- This report explores the current municipal-provincial fiscal framework in Saskatchewan and aims to assess if it is in line with the current economic and demographic realities of the province.
- Urban areas account for a large and growing share of Saskatchewan’s population, output, and employment.
- Saskatchewan’s municipal-provincial fiscal framework tends to favour rural areas over urban ones, and thus policy reform is warranted.

Saskatchewan—the land of lentils, wheat, and plains as vast as the eye can see—has undergone significant changes over the past number of decades. Agriculture will remain important to the provincial economy over the long term, thanks to a growing global population and economic development in emerging countries. Strong productivity growth in agriculture has allowed the province to remain Canada’s “bread basket”, but it has also greatly reduced the need for farm workers and has pushed people to move away from rural parts of the province.

A similar story is unfolding in Saskatchewan’s mining industry, another rural-oriented sector. Mining represents a significant portion of the province’s economic output, and an even larger share of merchandise exports, and will likely continue to do so. But it is a very capital intensive industry, and growing more so by the day. As such, its share of total employment, though until recently growing, is relatively small. In fact, only a little more than 4 per cent of the province’s workers are employed in mining.

Both of these trends point to the growing role of urban municipalities in driving economic growth. Indeed, the migration of people from rural areas to urban areas is the defining characteristic of urbanization, a process that has occurred or is occurring in most of the world, including in Saskatchewan. In fact, the share of the province’s population that resides in urban areas (cities, towns, villages, and resort villages) increased from 16 per cent in 1901 to 77 per cent in 2016.<sup>2</sup>

Urban areas share of Saskatchewan’s economic activity has been increasing alongside their share of the province’s population. Indeed, cities, villages, and towns now account for the lion’s share of output, population, and employment in Saskatchewan. In fact, Regina and Saskatoon alone together account for more than half of provincial output and employment.

Although a portion of economic activity in urban areas is directly and indirectly tied to mining and agriculture, resource extraction requires the ingenuity of highly-skilled workers in such fields as engineering and geology, and most of these workers live and work in cities, towns, and villages. Head

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<sup>2</sup>Urban areas include all cities, towns, villages, and resort villages in Saskatchewan. All other areas are considered rural.

office functions and other related services sector activity of these resource extraction firms also tend to take place in urban centres.

Such activity is part of a wider trend of the rising prominence of the services sector. This has had a major impact on both urban and rural municipalities in Saskatchewan. Many urban municipalities, particularly Regina and Saskatoon, have experienced much faster population and economic growth than the province as a whole in recent years.

This strong growth has increased pressure to increase spending on municipal infrastructure and services which, in turn, has strained local budgets. These pressures make it more difficult for urban municipalities to attract and retain business investment and people, both crucial ingredients for success in a hyper-competitive global economy.

On the other hand, many rural municipalities are struggling with the opposite problem: weak population growth and, in some circumstances, even declining population. This makes it difficult for these municipalities to generate sufficient revenue to help fund the maintenance and expansion of Saskatchewan's transportation infrastructure, which is crucial to getting the province's goods to domestic and international markets.

Given this context, the Saskatchewan Urban Municipalities Association (SUMA) commissioned The Conference Board of Canada to produce a report that explores the extent to which urban and rural municipalities in Saskatchewan possess the necessary fiscal tools to support economic growth and prosperity and to tackle the pressures they are facing in Saskatchewan's changing economic landscape. In other words, the report attempts to answer the following questions: Do urban municipalities have the fiscal capacity to foster sustainable growth? Will they be able to attract and retain business investment and people? Do rural municipalities have the fiscal capacity to help maintain and expand the transportation network? In other words, has Saskatchewan gone far enough to realign its suite of public policies to succeed in the 21<sup>st</sup> century economy?

More specifically, this report will show that the current provincial-municipal fiscal framework in Saskatchewan favours rural municipalities over urban ones, which is out of step with recent demographic and economic changes as well as the Saskatchewan Plan for Growth. Thus, this report concludes with recommendations for addressing this imbalance, which should help the province's economy to better adapt and prepare for challenges as well as to promote opportunities for growth and diversification. Our recommendations are also sensitive to the difficult fiscal situation that the provincial government currently faces.



## 2. Urbanization Trends

### Chapter Summary

- Canada, like most of the rest of the world, continues to urbanize; currently 82 per cent of its population resides within urban areas.
- Productivity, education, and opportunity are key aspects fueling the growth of urban areas in Canada.
- Fast population growth goes hand in hand with higher costs for municipalities. Yet, population increases do not necessarily result in corresponding increases in revenue. Fiscal pressures are rapidly arising from this situation.

This chapter provides a brief overview of trend of urbanization in Canada and across the globe, which is an important first-step in determining the needs and concerns of rural and urban municipalities across the country. Because this urbanization trend has been mirrored in all the provinces, this analysis will establish a base from which to explore the demographic and economic situation of Saskatchewan in subsequent chapters.

### 2.1.Recent Urbanization Trends

Urbanization has defined economic activity across the world for over two centuries now. The first major urbanization trends started in 18<sup>th</sup> century England with the emergence of the modern manufacturing industry, gains in sanitation, and higher agricultural productivity.<sup>3</sup> Since then, urbanization has become even more prominent across the world: according to the OECD, the world's urban population is projected to increase from less than 1 billion in 1950 to roughly 6 billion by 2050.<sup>4</sup> Today, as shown in Figure 1, Canada—just like all the other G8 countries—is highly urban, as 82 per cent of the population lived in an urban area in 2016.<sup>5</sup> This rate has steadily increased since 1851, when it was just above 10 per cent.<sup>6</sup>

The urbanization trend has continued, despite a falling share of manufacturing employment, thanks to the concomitant rise of services, another sector that derives significant benefits from locating in dense urban areas. As a result, urban areas continue to be more profitable for both people and firms, accounting for their mutual attraction.

People and firms accept the higher costs associated with living and doing business in urban areas because the benefits are even greater.<sup>7</sup> One way to quantify the benefits of urban areas is to compare labour productivity levels in cities with the rest of the country. Indeed, Figure 2 shows that the combined labour productivity level in 13 major Canadian metro areas, including Regina and Saskatoon, exceeds the level in

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<sup>3</sup> Organization for Economic Cooperation and Development, *The Metropolitan Century: Understanding Urbanization and its Consequences*. 20.

<sup>4</sup> Ibid. 11.

<sup>5</sup> Press, "Census 2016: Big cities home to big share of 35 million Canadians"

<sup>6</sup> Statistics Canada, *1851-2011 Census of the Population*.

<sup>7</sup> Arcand, "The Growing Importance of Cities."

the rest of the country. In other words, the average urban worker produces more output per hour than an average rural worker.

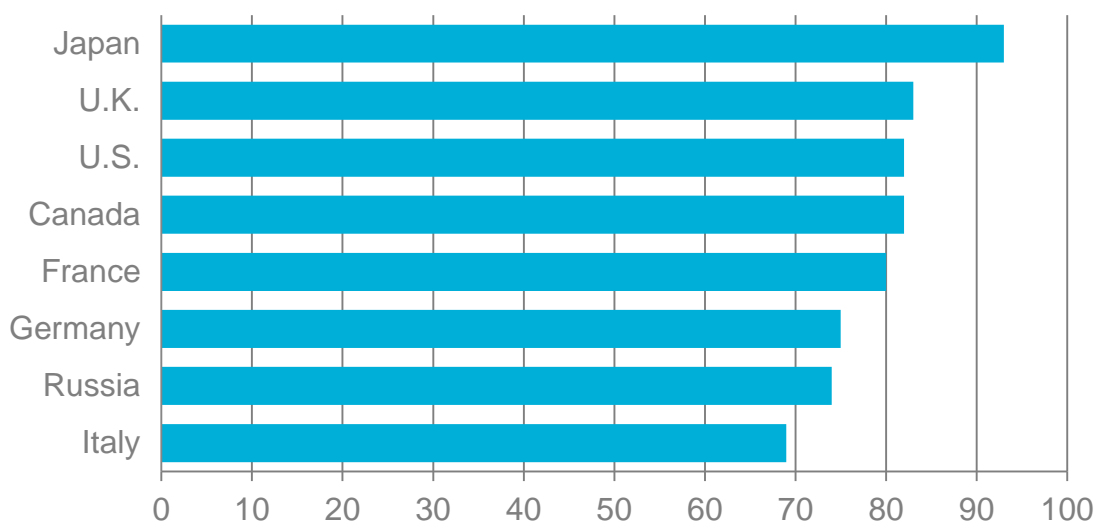
Another benefit of living in dense urban areas is that it increases the rate at which ideas are created and exchanged among individuals and firms, thus speeding innovation.<sup>8</sup> Moreover, transport and communications costs are lowered when people and firms locate near one another together in cities and industry clusters. Such benefits are known as “agglomeration economies.”<sup>9</sup>

Higher productivity levels and other agglomeration economies result in higher wages for workers and higher profits for firms. In 2015, workers in the 13 Canadian metropolitan areas featured in Figure 2 earned 20 per cent more labour income than people in the rest of the country.<sup>10</sup> This finding is observed internationally: per capita incomes are almost four times higher in those countries where a majority of people live in cities than in those countries where most people live in rural areas.<sup>11</sup>

Figure 1

### The G8 Countries Are Largely Urban

proportion of the population living in an urban area, 2015 or 2016



Source: The World Bank, “Urban population (% of total)”.

<sup>8</sup> Ibid.

<sup>9</sup> Ibid.

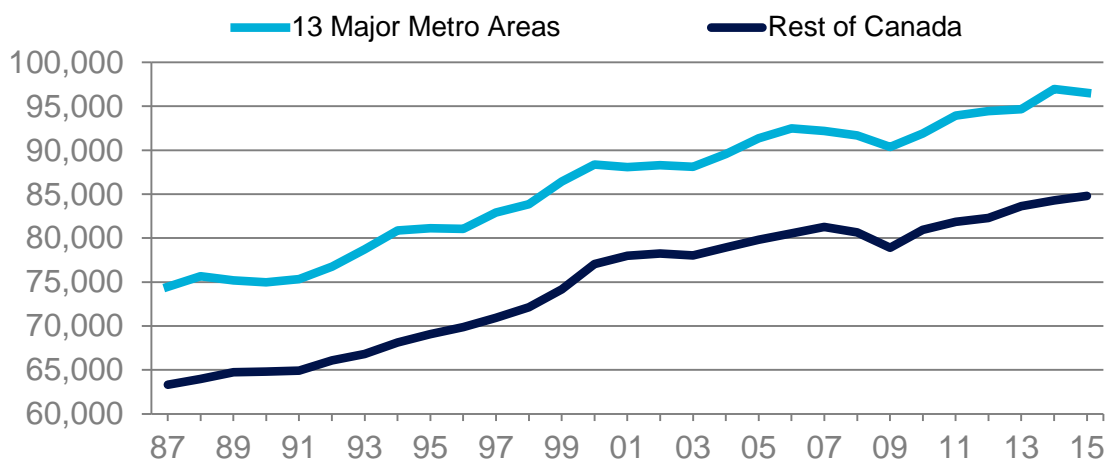
<sup>10</sup> Ibid.

<sup>11</sup> Glaeser, *Triumph of the City: How Our Greatest Invention Makes Us Richer, Smarter, Greener, Healthier and Happier*, 6.

Figure 2

**Cities are More Productive**

Real output per worker (1987-2015)



Halifax, Québec City, Montréal, Ottawa, Toronto, Hamilton, Winnipeg, Regina, Saskatoon, Calgary, Edmonton, Vancouver, Victoria

Source: The Conference Board of Canada.

As well, the importance and appeal of big cities in Canada is illustrated by the large share these cities make up of their province’s gross domestic product (GDP), as shown in Table 1. In fact, Canada’s largest census metropolitan areas account for a higher share of output than population in each of their respective provinces. For example, in 2015, Regina and Saskatoon accounted for 48.2 per cent of Saskatchewan’s population, but contributed 53.5 of the province’s GDP.

Table 1

Province	CMA(s)	Share of provincial GDP, 2015	Share of provincial population, 2015
Nova Scotia	Halifax	55.8	44.3
Quebec	Montréal	53.0	49.2
Ontario	Toronto	51.9	44.5
Manitoba	Winnipeg	67.0	61.4
Saskatchewan	Regina and Saskatoon	53.5	48.2
Alberta	Calgary and Edmonton	68.6	66.9
British Columbia	Vancouver	59.0	53.5

Source: The Conference Board of Canada.

## 2.2. Education and labour opportunities: a key factor

The high rate of urbanization in Canada is further explained by the number and diversity of opportunities that urban areas offer. These start with a higher number of educational institutions (universities, colleges, technical schools, etc.) than rural municipalities. This helps explain the higher level of educational attainment in urban centres. Indeed, the number of people with bachelor degrees in the 13 metropolitan areas featured in Figure 2 is more than double of that in the rest of the country.<sup>12</sup> This is also true for individuals holding graduate certificates, diplomas or degrees. In Regina and Saskatoon, the number of people with bachelor degrees is 1.9 times higher than in the rest of the province. The ratio is 2.7 for individuals with graduate certificates, diplomas or degrees.<sup>13</sup>

This is highly relevant since the information and communications technology (ICT) revolution has rapidly boosted Canada's proportion of knowledge-based jobs in the last three decades (see Figure 3). Knowledge-based jobs are jobs that are directly related to the production, distribution and use of knowledge and information. The rising importance of such jobs is characterized by an increasing demand for more highly-skilled workers, often ones with university degrees or college diplomas. Hosting multiple educational institutions is therefore a great advantage for a municipality, as it will help attract more of these individuals. Reinforcing this notion is the idea that firms locate near their key factors of production, which in a knowledge-based economy is a skilled workforce. Accordingly, the presence of highly-skilled individuals—tied to the availability of higher education and the ability to attract highly-skilled migrants— attracts firms, which in turn attracts more high-skilled individuals, creating a virtuous circle.

The good news for urban municipalities is that, because of their higher concentration of businesses, industry clusters, and educational institutions, it makes it easier to connect high-skilled and educated individuals with the firms looking for such specialized workers. Urban municipalities achieve this by reducing the physical space between people and firms through job fairs, seminars, conferences, and university career services, but also sometimes through informal means.

True, some have argued that the expansion of ICT, which has vastly reduced communication costs, has reduced the need for face-to-face contact and thus the benefits of living in dense urban areas. However, the global trend of urbanization continues apace, suggesting the effect could be the exact opposite. It appears that the ICT revolution is actually increasing, not decreasing, the benefits of proximity. This is because electronic communication and face-to-face communication are complements, not substitutes.<sup>14</sup> Hence, as the quantity of one increases, so will the demand for the other. Indeed, as transmitting information becomes more efficient, we spend more, not less, time transmitting information.

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<sup>12</sup> Arcand, "The Growing Importance of Cities".

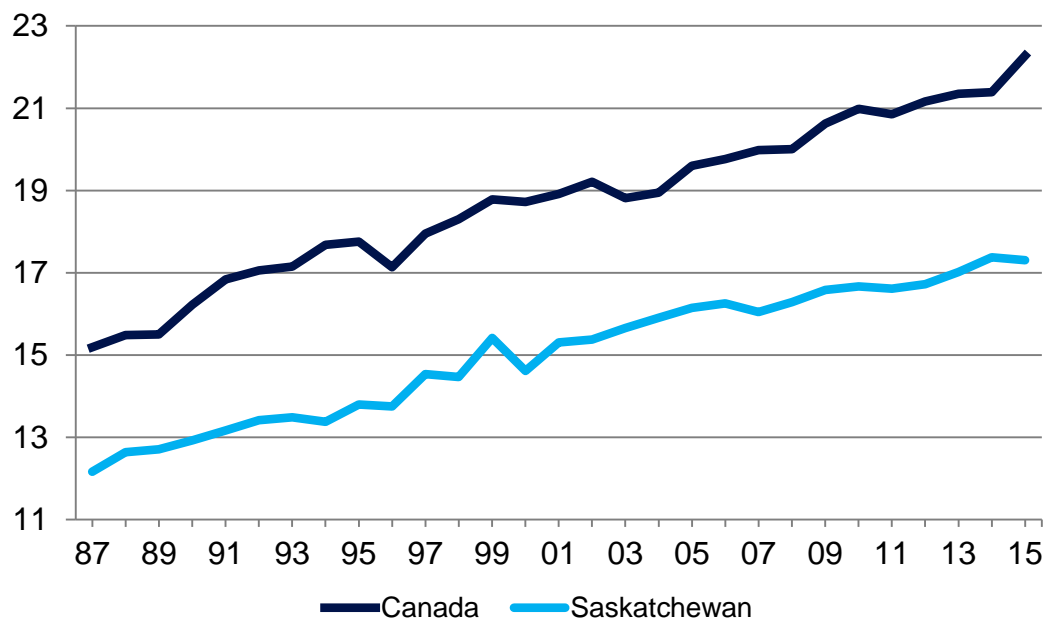
<sup>13</sup> Statistics Canada, *National Household Survey 2011*.

<sup>14</sup> Arcand, "The Growing Importance of Cities".

**Figure 3**

**Knowledge-Based Jobs**

Canada (1987-2015, per cent of total)



Source: The Conference Board of Canada.

**2.3. Quality of life**

Aside from education and employment, quality of life is another factor that people consider when they choose where to live. Many people are attracted to urban centres that offer a large array of recreational, cultural, and entertainment options, including public parks, swimming pools, ice hockey rinks, restaurants and bars, concert halls, and museums. In this sense, cities, towns, and villages are “urban playgrounds” where people have fun, interact, and form relationships. Interestingly, holding income, education, marital status and age constant, relative to rural residents, city residents are: 19 per cent more likely to go to a rock or pop concert, 26 per cent more likely to have a drink at a bar, 44 per cent more likely to visit a museum, and 98 per cent more likely to go to a movie theatre.<sup>15</sup> Urban residents clearly take advantage of these services, most likely because they are proximate.

**2.4. Immigration**

Another factor behind the country’s high urbanization rate is Canada’s shifting demographic landscape. Immigration has become a major source of population growth, representing about 70.2 per cent of the population increases between 2000 and 2016.<sup>16</sup> Both population aging—16.6 per cent of the country’s population is aged 65 and above, a share expected to hit 24 per cent by 2035<sup>17</sup>—and low fertility rates explain this changing growth underpinning. This is relevant because immigrants overwhelmingly live in

<sup>15</sup> Ibid.

<sup>16</sup> The Conference Board of Canada, *National database*.

<sup>17</sup> The Conference Board of Canada, *A Long-Term View of Canada’s Changing Demographics: Are Higher Immigration Levels an Appropriate Response to Canada’s Aging Population?*

urban municipalities, particularly those that offer good job opportunities, established ethnic communities, and settlement and integration services.

### **2.5. Costs Cannot be Ignored**

Urban areas that offer these benefits tend to enjoy above average population growth. Such population pressures have significant costs. Bigger urban centres must manage higher infrastructure costs, expansion, maintenance and repair, as well as higher demand for services such as police and firefighting, public transit, and affordable housing.

Unfortunately, Canadian urban municipalities tend to not have the revenue tools needed to cover these costs. Their main source of revenue is the property tax, but revenue generated from this tax does not necessarily grow in line with the economy, but is more closely tied to the health of the real estate market. This is why the Conference Board has for many years argued that municipalities should be given access to other revenue sources that grow more in line with the wider economy, such as income and sales taxes. While there has been movement on this front—municipalities receive a share of the revenue from the federal gas tax—more needs to be done.

### 3. Demographic and Economic Trends in Saskatchewan

#### Chapter Summary

- Saskatchewan has seen rapid population growth in recent years. Most of this growth is happening in urban areas: 77 per cent of the province's population now lives in a city, town, village or resort village.
- Agriculture's share of total employment continues to fall, while mining's share remains low, limiting the need for people to live and work in rural areas.
- In contrast, the services sector continues to rise in importance, especially knowledge-based jobs that require high skills, which is fueling growth in urban areas.

This chapter assesses demographic and economic trends in Saskatchewan and the resulting impact on municipalities' fiscal capacity. Since Saskatchewan agriculture and mining play significant roles in the economy, it is unsurprising that the province's urbanization rate is somewhat below the Canadian average. Still, the province has seen strong urban growth in recent years. Reviewing the factors underpinning this growth and the economic structure and trends of rural and urban areas will shed light on the provincial outlook and support our contention that Saskatchewan's current provincial-municipal fiscal arrangement needs reform.

#### 3.1. Saskatchewan's demographics

Saskatchewan's population has grown remarkably in recent years. After decades of timid increases and even declines, the province's population grew at an average annual rate of 1.6 per cent from 2009 to 2016,<sup>18</sup> trailing only Alberta among Canada's provinces. This compares to average annual national growth of 1.1 per cent. By the end of 2016, the province's population exceeded 1.09 million, up from 968,000 ten years earlier, an increase of some 130,000 people.<sup>19</sup> In order to better understand the effects of this strong growth, and its future consequences, it is helpful to break down the headline number into its main components—net migration (international and interprovincial) and the natural increase (births minus deaths).

The province's natural increase has climbed fairly steadily over the past ten years. The number of births rose from about 12,500 in 2006-07 to nearly 16,000 in 2015-16. The number of deaths have also increased, but at a much slower rate. As a result, the natural increase rose from just 3,500 people in 2006 to over 6,000 people in 2015-16. There have been three main drivers behind the rise in the natural increase. First, the number of Saskatchewan women in their prime childbearing years (those aged between 15 and 39 years) has been increasing.<sup>20</sup> Second, the fertility rate in the province has also risen considerably from 1.8 births per woman in 2000 to 2 births per woman in 2012,<sup>21</sup> the highest amongst Canadian provinces.<sup>22</sup>

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<sup>18</sup> The Conference Board of Canada and Statistics Canada, *Cansim Table 051-0001*.

<sup>19</sup> Government of Saskatchewan, *Census Population 1986-2016*.

<sup>20</sup> *Sask Trends Monitor, February 2015*.

<sup>21</sup> The Conference Board of Canada and Statistics Canada, *Cansim Table 102-4505*.

<sup>22</sup> The Conference Board of Canada, *Provincial Outlook 2016: Long-Term Economic Forecast*.

Finally, the province is aging at a slower pace than Canada as a whole: the share of individuals aged 65 and over increased by 2.4 per cent from 2010 to 2016 in Canada, but only by 0.4 per cent in Saskatchewan.<sup>23</sup>

At the same time, net immigration has increased sharply in recent years, suggesting the province is growing in popularity as a landing spot for immigrants (Figure 4). Net immigration averaged only 1,300 people per year between 1995-96 and 2000-07, but the annual average jumped to nearly 12,500 people over the past five years. The other source of net migration—interprovincial migration—has been an overall drain on population growth over the past five years, albeit only moderately.

It is expected that these demographic trends will extend into the foreseeable future. The Conference Board forecasts that net migration's contribution to population growth in Saskatchewan will continue to outpace the natural increase in the province. Indeed, net migration should increase steadily until 2037, when it will add almost 9,000 people to the province. On the other hand, the province's natural increase should remain steady in the medium term and then slowly decline until 2037, when it will add about 4,700 people to Saskatchewan.

Moreover, the importance of immigration is also growing because immigrants are getting younger. The proportion of immigrants aged 0-39 in 2015-16 was 82.6 per cent, an increase from 78.7 per cent in 2005-06.<sup>24</sup> Immigrant women account for half of this age group, thus contributing to Saskatchewan's natural increase. This helps rejuvenate both the population and the work force in the province. Meanwhile, the proportion of all Saskatchewan residents aged 0-39 has remained fairly stable, ranging between 52.4 and 54 per cent over the same period.<sup>25</sup>

The recent increase in immigration is arguably the most dominant demographic trend in the last decade, a turning point from 1915-2001 when the number of immigrants and non-permanent<sup>26</sup> residents declined steadily both absolutely and as a percentage of total population. After reaching a record low in 2001, immigration began a steady increase, so by 2011 immigrants represented 7.6 per cent of Saskatchewan's population.<sup>27</sup> Since then the number of international immigrants has continued to rise and together with non-permanent residents, this group represented close to 15 per cent of the population last year.<sup>28</sup> This is key because this new wave of immigrants is fundamentally different from the ones that came to the province in the 20<sup>th</sup> century. Newcomers are now younger, and are economic immigrants, rather than refugees. The majority of immigrants are thus skilled workers, a key demographic to spur economic growth.

Finally, it is important to track newcomer's mobility, as they can land in a province and subsequently move elsewhere within the country. In Saskatchewan, the retention rate seems to have improved; among the

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<sup>23</sup> The Conference Board of Canada and Statistics Canada, *Cansim Table 051-0001*.

<sup>24</sup> The Conference Board of Canada and Statistics Canada, *Cansim Table 051-0011*.

<sup>25</sup> The Conference Board of Canada and Statistics Canada, *Cansim Table 051-0001*.

<sup>26</sup> Non-permanent residents include foreign workers, foreign students, refugee claimants, and any other persons granted the right to live in Canada on a temporary basis.

<sup>27</sup> Sask Trends Monitor, *February 2016*.

<sup>28</sup> *Ibid.*

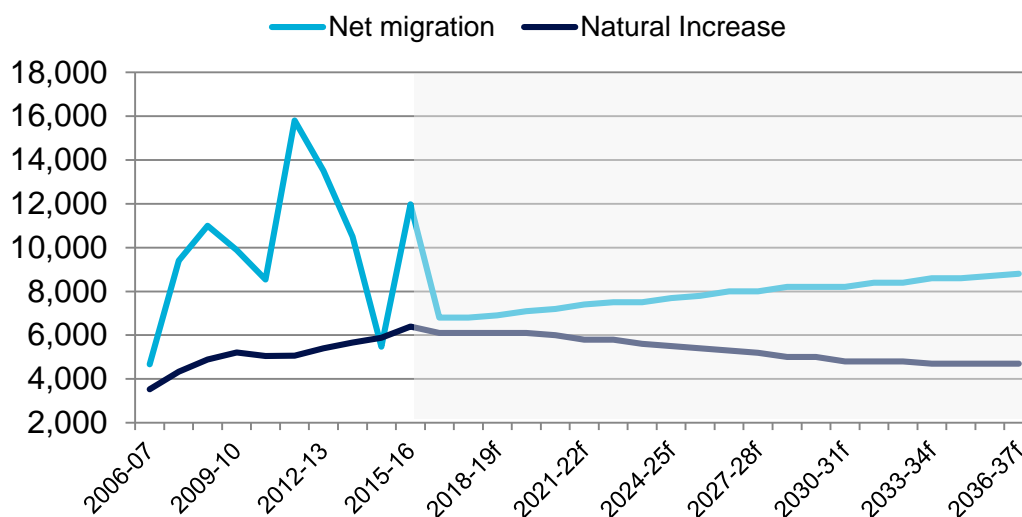


landed immigrants of the late 1990s, only one-third were still in the province 15 years later; among those that came in the early 2000s, half remained in the province after ten years; among those arriving after 2007, about 80 per cent were still in the province after five years.<sup>29</sup>

Figure 4

### Migration Will Continue to Drive Growth

Components of population growth, Saskatchewan (2006-2035)



Source: Statistics Canada and The Conference Board of Canada, Table 051-0004

### 3.2. Urbanization in Saskatchewan

Even though urbanization has followed similar trends across all provinces, varying provincial economic activity prompts significant differences. In Saskatchewan, the resources sector, including agriculture and energy, has accounted for an important part of economic activity, so the province’s urbanization rate is still somewhat below the Canadian average. However, Saskatchewan is not immune to industrialisation and the rise of the service economy, and consequently, urbanization. In fact, as Figure 5 shows, the share of the urban population (cities, towns, villages, and resort villages)<sup>30</sup> rose from 16 per cent 1901 to 77 per cent in 2016.<sup>31</sup> Most of the province’s population growth is occurring in its urban centres; in 2016, Saskatchewan’s cities alone accounted for 60 per cent of the province’s population.<sup>32</sup> These 17<sup>33</sup> cities posted strong population gains between the two most recent Censuses, with average annual growth of 1.9 per cent between 2011 and 2016. Population growth was especially strong in Warman (9.2 per cent per year on average), Martensville (4.6 per cent per year on average), Lloydminster<sup>34</sup> (3.8 per cent per

<sup>29</sup> Ibid.

<sup>30</sup> Figures include all cities, towns, villages, and resort villages in Saskatchewan

<sup>31</sup> Government of Saskatchewan, *Saskatchewan Census Population*.

<sup>32</sup> Ibid.

<sup>33</sup> Flin Flon’s Saskatchewan portion included.

<sup>34</sup> Saskatchewan part only.

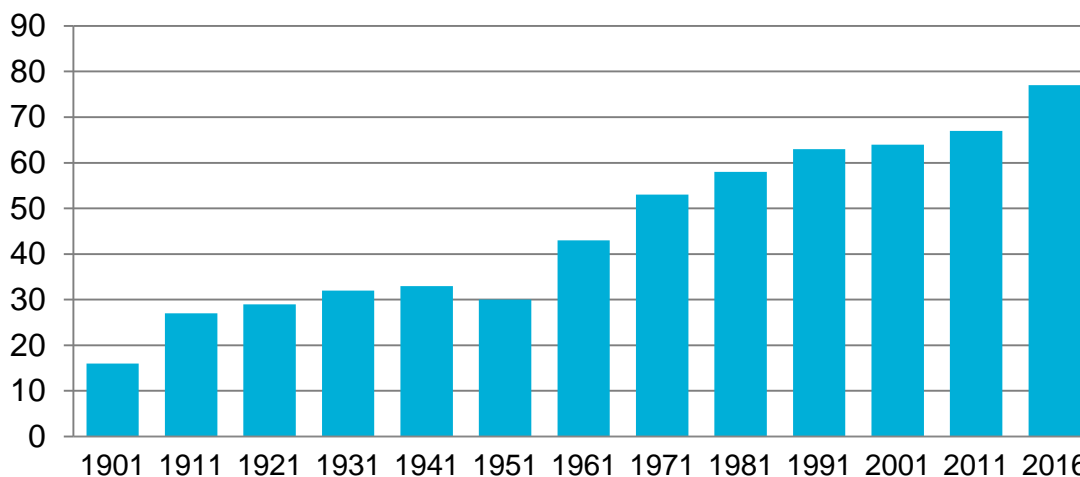
year on average), Regina (2.1 per cent per year on average), and Saskatoon (2.2 per cent per year on average). In comparison, the overall province saw its population climb by 1.2 per cent per year over the same period.

Net international migration contributes to urbanization since most immigrants choose to live in cities. On average, over 70 per cent of the province's international immigrants have chosen to live in Regina and Saskatoon alone since 2001.<sup>35</sup> In 2011, 84 per cent of immigrants to the province took up residence in a major urban centre.<sup>36</sup> Given that immigration now outweighs the natural increase as the biggest source of population growth, we expect the province to continue urbanizing at a steady rate. Significantly, the majority of these immigrants are of working age or younger, hence, we also expect labour force growth to be much stronger in urban centres.

**Figure 5**

### Saskatchewan Still Urbanizing Too

Proportion of the population living in an urban area, 1901-2016



Source: Government of Saskatchewan, Saskatchewan Census Population

### 3.3. Saskatchewan's industries

These demographic shifts are tied to fundamental changes in the composition of the province's economy, as urbanization goes hand-in-hand with the move towards services. This change in the economic landscape of the province is in line with the ICT revolution and its fallouts, as described in section 2.2. Indeed, as the economy shifts towards the services industries, knowledge has become a key asset in the labour market. As shown in Table 2, most of the job creation in Saskatchewan has gone to workers with higher levels of educational attainment, usually found within urban areas of the province. From the net 51,800 jobs created in the province from 2009 to 2016, 43,400 jobs went to those detaining bachelor's degrees or higher and 21,700 went to those with post-secondary certificates or diplomas. On the other

<sup>35</sup> The Conference Board of Canada and Statistics Canada, *Cansim Tables 051-0004 and 051-0057*.

<sup>36</sup> Johnson-Shoyama Graduate School of Public Policy, *The State of Saskatchewan Cities*.

hand, individuals with some post-secondary education lost 10,300 jobs and those with a high school degree or less lost 3,000 jobs. Perhaps the most obvious example is agriculture—by definition a rural industry. Agriculture’s share of total output has shrunk steadily since the 1960s, strongly correlated with soaring urbanization across the province. In the early 1960s, agriculture accounted for as much as 17.7 per cent of provincial GDP, but its share fell to 6.4 per cent last year.<sup>37</sup> That said, its share of total output appears to have stabilized around this share, as can be seen in Figure 6. On the other hand, the share of economic activity generated by industries strongly linked to urban centres, like manufacturing, wholesale and retail trade, and finance, insurance and real estate has increased or remained stable over the years (Figure 7).

**Table 2**

Attainment	Job Gains/Losses
All levels	51,800
Bachelor and above	43,400
Post-secondary certificate or diploma	21,700
Some post-secondary education	-10,300
High school or less	-3,000

Source: Statistics Canada, 2011 National Household Survey

The steep drop in agriculture’s share of provincial output over the past five decades does not mean that farm owners and operators have struggled. True, total farmland in the province fell by about 2.5 million acres between 1981 and 2011, and the number of farms in Saskatchewan decreased at an even faster rate, implying that the average size per farm increased from 952 acres to 1,668 acres. Yet, farmers’ fiscal situation appears strong.

For example, the 2011 Census of Agriculture showed that 13 per cent of farms reported \$500,000 or more total gross receipts, up from 4 per cent in 2005. Similarly, 42 per cent of farms reported at least \$1 million of total farm capital (compared to 25 per cent in 2005), and Saskatchewan’s gross farm receipts increased by 10 per cent in 2005-10, more than double the increase for the rest of Canada (4 per cent).<sup>38</sup> This is to be expected, as fewer and larger farms are able to capture a larger market share, effectively improving their financial situation. Hence, the decrease of agriculture’s share of total output is the result of other industries expanding faster than agriculture, not a decline in agricultural GDP. In fact, real output in crop and animal production has been showing a clear upward trend since the early 2000s.

<sup>37</sup> The Conference Board of Canada, *Provincial database*.

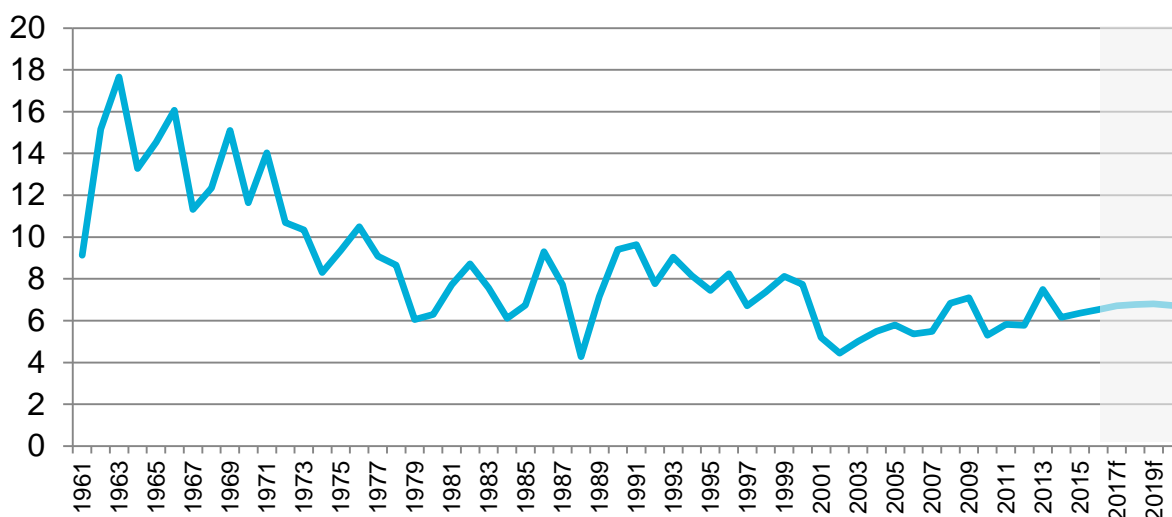
<sup>38</sup> Statistics Canada, *2011 Census of agriculture*.

However, one major area of concern is the demographic profile of Saskatchewan’s farm population. In 2011, the average age of a farmer in Saskatchewan was 54 years old, compared to a median age of 38.2 years old for the entire provincial population. Furthermore, almost half of all farmers in the province were aged 55 years old and over, while only 9 per cent of total farmers were under 35 years old.<sup>39</sup> Additionally, farmland values have increased at a fast pace in Saskatchewan, a factor that may deter young growers from purchasing land. And even without considering these financial constraints, there is simply a smaller cohort of young operators available to take over from a much larger group of older operators that is fast approaching retirement.<sup>40</sup>

**Figure 6**

**Agriculture's Importance Stabilizing**

Share of real GDP in Saskatchewan (per cent)



Source: The Conference Board of Canada.

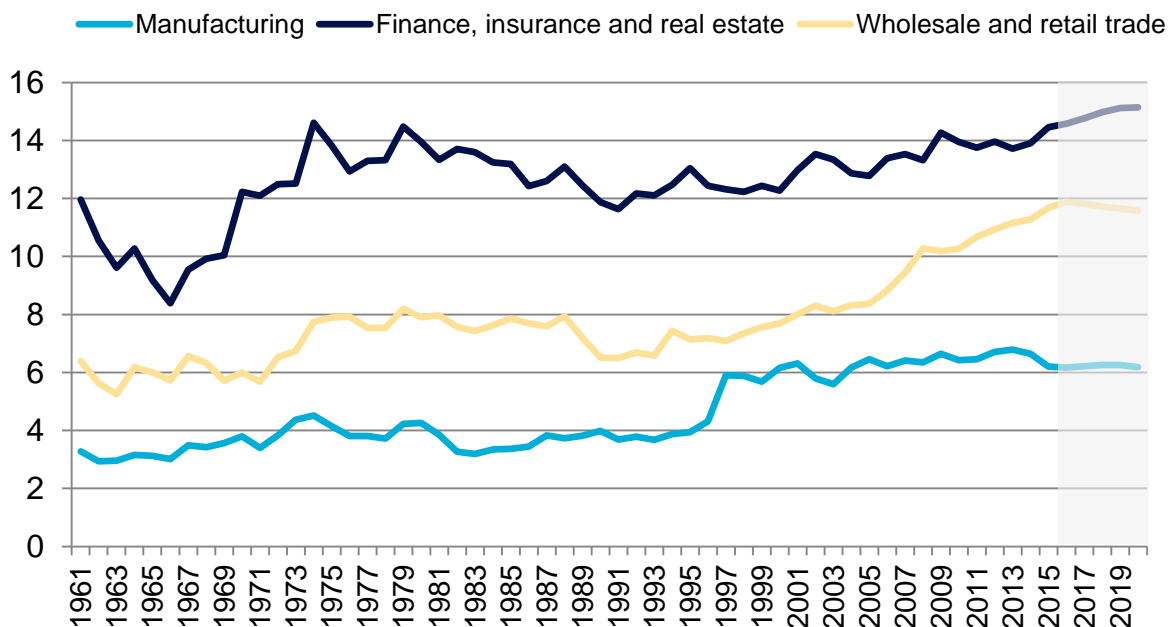
<sup>39</sup> Ibid.

<sup>40</sup> Statistics Canada, *Demographic Changes in Canadian Agriculture*.

Figure 7

**Other Selected Industries**

Share of GDP, SK (per cent)



Source: The Conference Board of Canada.

Along with output, agriculture’s share of Saskatchewan employment has dramatically decreased since the mid 1970s, falling from 1 in 4 jobs in 1976 to fewer than 1 in 10 jobs in 2015 (see Figure 8).<sup>41</sup> In fact, agriculture employment has also declined in absolute terms. Some 86,000 people were employed in this industry in Saskatchewan in 1981, but that fell to just over 41,000 in 2015, a decline of over 50 per cent. Given that output has continued to rise, it is a clear indication that the agriculture sector has enjoyed tremendous productivity gains over the past 34 years. Indeed, advances in technology have led to both rising crop yields and crop intensity, which in turn, have greatly reduced the need for labour.

These trends highlight the fact that urbanization has been caused by both push and pull factors. The decline of agricultural employment pushed people to move urban areas to seek work, while at the same time, being attracted by urban amenities and activities. The end result is a rural population with an older demographic profile. The 20-44 age group accounts for only 27 per cent of the rural population (2011), while this same group represents 36 per cent of the population in urban areas.<sup>42</sup>

Moreover, the rise of immigration as the dominant source of population growth is another trend that favours urban areas over rural ones, given that the vast majority of immigrants live in urban centres.

<sup>41</sup> The Conference Board of Canada, *Provincial database*.

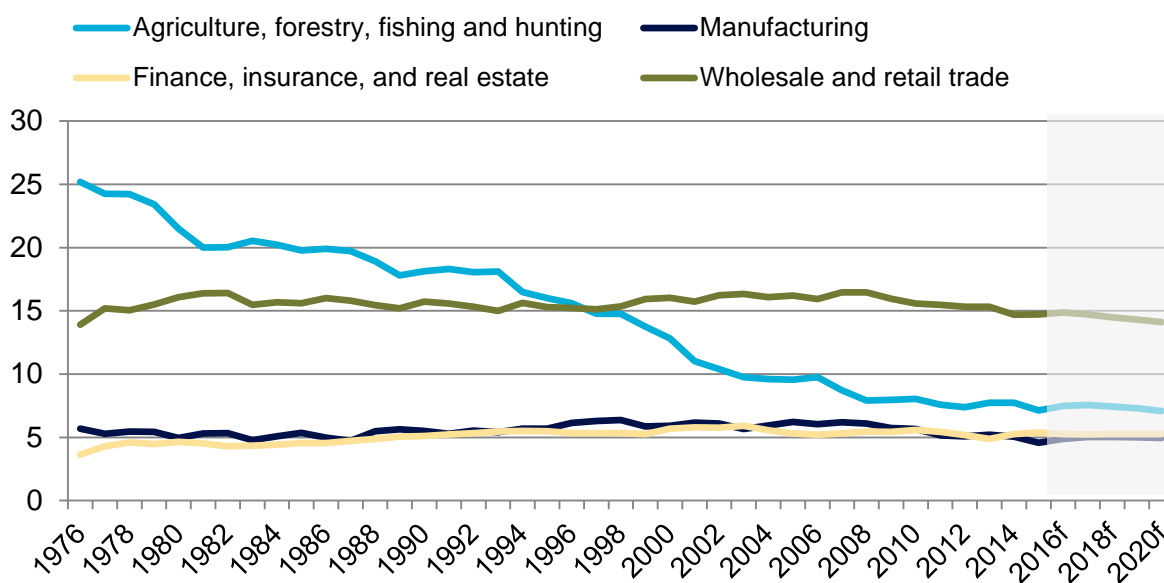
<sup>42</sup> The Canadian Rural Revitalization Foundation, *State of Rural Canada 2015*.

Indeed, even though their share of total employment is still small (13 percent in 2015), immigrants accounted for 75 per cent of Saskatchewan’s overall employment growth between 2009 and 2015.<sup>43</sup>

Figure 8

**Employment Following Similar Trends**

Share of total employment, SK (per cent)



Source: The Conference Board of Canada.

**3.4. Mining and Oil and Gas**

Direct activity from mining and oil and gas, another key sector in Saskatchewan, also tends to occur in rural areas, though some potash mines are located within the boundaries of some census metropolitan areas. Products from this industry account for a large share of Saskatchewan’s exports. Indeed, Saskatchewan’s top two exports in 2015 were crude petroleum oils and oils obtained from bituminous minerals and potassium chloride (potash), accounting for 42.9 per cent of the total value of the province’s merchandise exports.<sup>44</sup> And even with the current slump in oil and other commodities prices, this industry’s share of provincial GDP remains fairly high at around 20 per cent. Although this sector’s share of output has been trending downward, it remains and will remain a significant part of the provincial economy, and the key linkages between it and urban economic activity will persist.

Indeed, technological advances are also integral to the mining and oil and gas extraction sector, and this has implications for the type of occupations in demand. For example, tools like aerial satellite imagery and imaging sensor systems are important in natural resource extraction because they allow the collection of information before digging or drilling begins. It is now possible to fit aircrafts and satellites with sensors

<sup>43</sup> Sask Trends Monitor, February 2016.

<sup>44</sup> Industry Canada, Trade Data Online.

that use the spectral properties of materials to identify them.<sup>45,46</sup> The use of technology requires more skilled workers—like engineers, geologists, and chemists—for research and development projects. Generally, such workers, along with most other industry employees, are housed in Saskatchewan’s urban areas. So, along with head office workers and employees of other service firms indirectly tied to the mining and oil and gas industries, such as lawyers and accountants, the occupations growing in demand also tend to be located in urban centres. This makes urban centres fundamental to the progress of the mining and oil and gas sector in Saskatchewan.

To further illustrate the link between the mining industry and urban municipalities, we used an Input-Output Model from 2010<sup>47</sup> to show the supply chain impacts of a \$1.4 billion increase in potash mining output—equivalent to the average annual output from 2011 to 2015. The results include notable boosts to industries clustered in urban areas, like wholesale trade, finance, insurance, and real estate, legal, accounting, bookkeeping and payroll services, computer systems design and related services, and management of companies and enterprises, to name a few. For example, the \$1.4 billion increase in potash mining output produces a \$4.9 million increase in computer systems design and related services output. Other supply chain impacts can be found in Table 3.

**Table 3: Selected supply chain impacts of a \$1.4 billion increase in potash mining output.**

Industry	Impact on GDP	Impact on Employment <sup>1</sup>
Wholesale trade	169,206,417	1,513
Finance, insurance, and real estate	48,715,148	494
Management of companies and enterprises	13,459,952	216
Administrative and support services	11,669,408	340
Retail trade	7,841,348	216
Telecommunications except cable and other program distribution	7,409,148	62
Computer systems design and related services	4,908,561	93
Other professional, scientific and technical services	4,538,103	93
Legal, accounting, bookkeeping, payroll, and tax preparation services	4,136,774	62

<sup>1</sup> Includes full-time, part-time and/or temporary jobs.

Source: The Conference Board of Canada, Statistics Canada.

All told, the urbanization trend continues in historically rural-based Saskatchewan, although the share of people in its cities, towns, and villages remains slightly below the Canadian average. The rise in the number of skilled immigrants, who predominantly choose to live in urban areas, the development of urban centres as industrial, commercial, and educational and health care hubs, and the relative decline of

<sup>45</sup> Partridge and Olfert, “The Winners’ Choice: Sustainable Economic Strategies for Successful 21st Century Regions”.

<sup>46</sup> Gayton, “Farming From Space”.

<sup>47</sup> The Conference Board of Canada, *Footprint on Potash*.

agriculture compared to urban-based industries—like manufacturing, wholesale and retail trade, and finance, insurance, and real estate—helps explain why urban centres have recently experienced such strong growth. As such, it is important to study the capacity of urban centres to sustain their growth, maintain their infrastructure, and provide a high level of services and quality of life to their growing populations.



## 4. Saskatchewan's Urban Municipalities Facing Growth Pressures

### Chapter Summary

- Most tax exemptions in the province are not directly geographically-driven, although some are geared towards industries with strong ties to either urban or rural areas.
- Some of these exemptions aim to reduce the fiscal burden of a specific group, without trying to achieve an economic goal, increase fairness, or curb behaviours, with the farm fuel tax exemption being a prime example.
- Although municipalities have tools to shift the burden of property taxes from one property class to another, the provincial elements of the property tax formula give a fiscal advantage to rural properties.
- Although generous, the Municipal Revenue Sharing grant is heavily skewed in per capita terms toward rural municipalities.

This backdrop of rising immigration, mainly to urban centres, and economic diversification away from agriculture and towards services that puts a premium on skilled workers living in cities, towns, and villages raises important municipal finance questions. Do urban municipalities have the resources to ensure they are attractive and contribute to Saskatchewan's growth? Will local governments be able to provide the quality of life that urban residents demand? Do urban municipalities get their fair share of the fiscal pie?

Urban municipalities across the country are heavily reliant on property taxes as a source of revenue, which is intended to be a tax on wealth.<sup>48</sup> This made sense years ago when most wealth was accumulated in the form of property, and was especially true of farmland, where the value of property was very closely aligned with how much income the land could produce.<sup>49</sup>

But the focus on a tax that is so closely tied to property wealth is much less relevant in today's economy. Indeed, there is no longer a strong connection between ownership of property and wealth and income.<sup>50</sup> In other words, property taxes are not necessarily related to the ability to pay, which could be a burden for some homeowners, particularly low-income seniors. Indeed, the ability to pay fluctuates with changes in employment, family size, the economy, and age, all of which may not be reflected in the assessed value of a home.<sup>51</sup>

Another problem with property taxes is that they are also weakly connected to the services that municipalities provide, notably policing and firefighting, transportation, planning and development, and

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<sup>48</sup> Report of the Tax Reform Committee, *Creating a Modern Property Tax System for Halifax*, 4.

<sup>49</sup> Ibid.

<sup>50</sup> Ibid.

<sup>51</sup> Ibid.

public utilities.<sup>52</sup> This often leads to complaints that service delivery has not improved in tandem with increases in assessed property values.

Unfortunately, most municipalities in Canada do not have the fiscal authority to raise revenues through income or sales taxes, sources of revenue that tend to grow in line with the economy. Of course, the federal and provincial governments have the ability to levy these types of taxes.

Notwithstanding increased transfers from higher levels of government, including the transfer of PST revenue to municipalities in Saskatchewan, the heavily reliance on property tax revenue continues to put pressure on municipal infrastructure and services. In other words, it will become increasingly difficult for cities, towns, and villages across Saskatchewan and Canada to maintain per capita service levels and expand and maintain infrastructure. This may negatively affect quality of life, which is a major determinant of a city's attractiveness.

### 4.1. Tax Exemptions

Although most provincial fiscal measures favour neither rural or urban areas, certain specific tax expenditures and exemptions in Saskatchewan are clearly geographically-driven.

For instance, rural municipalities receive the full benefits of any tax exemptions targeted at the agricultural industry. Indeed, agriculture is barely present in urban municipalities. As an example, the census subdivision of Saskatoon was home to 0.1 per cent of all the province's farms in 2011.<sup>53</sup>

Among the provincial tax exemptions that specifically target the agriculture industry, the most notable ones are:

- 1) a tax exemption for farm machinery and repair, which cost \$164.7 million in forgone revenue in the last two fiscal years and is budgeted for an additional \$83.8 million in 2016-17;
- 2) a tax exemption for farming fuel, which has cost \$233.9 million in the last two fiscal years and is budgeted for another \$120.1 million in 2016-17; and
- 3) a tax exemption for fertilizer, pesticide and seed that has cost provincial taxpayers \$298.2 million over 2014-16, with another \$163.4 million budgeted for 2016-17.

These exemptions, which are illustrated in Figure 9, add up to a total of just over \$1 billion in foregone revenue for the province over the fiscal years 2014-15 to 2016-17<sup>54</sup>.

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<sup>52</sup> Ibid.

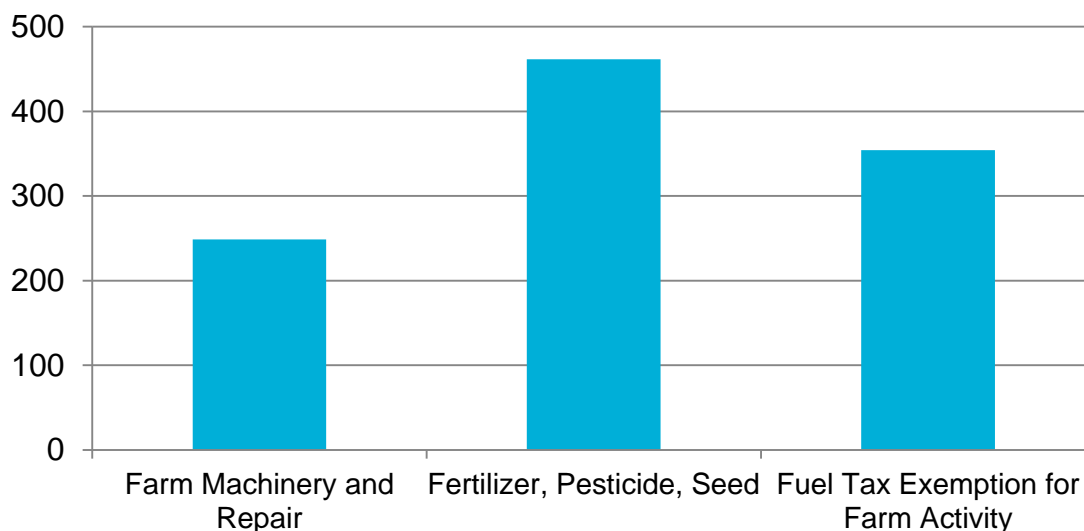
<sup>53</sup> Statistics Canada, *Cansim Table 004-0200*.

<sup>54</sup> Government of Saskatchewan, *2014-17 budgets*.

Figure 9

**RM Specific Provincial Tax Expenditures**

(Millions of nominal \$, 2014-16e)



Source: Government of Saskatchewan, The Conference Board of Canada.

One of these measures, the fuel for farm activity exemption has been criticized by Saskatchewan’s Auditor General for lacking a clear objective. In its 2016 report, the Office of the Provincial Auditor of Saskatchewan stated that “because (The Ministry of Finance) has not specifically determined what the fuel tax exemption program is designed to achieve—other than reducing taxes for eligible individuals or corporations—the Ministry does not know whether the fuel tax exemption program<sup>55</sup> is successful and continues to be needed.”<sup>56</sup>

In fact, the Ministry of Finance has expressly stated the program’s two objectives:

- 1) “To provide fuel tax relief to qualified farmers and primary producers for fuel used in their farming, commercial fishing, trapping, or logging activities with the understanding that the majority of fuel will be consumed off-road.”<sup>57</sup>
- 2) “To reduce the cost of fuel as a heating source, making it comparable with other sources such as natural gas (there is no tax on the purchase of natural gas).”<sup>58</sup>

While it can be argued that the second objective is clear, since it creates a level playing field in the tax treatment of different heating fuels—there is not an equivalent tax on natural gas—the program’s primary objective—tax relief for farmers—seems less valid. In fact, the rationale behind tax exemptions is to enhance fairness or to promote certain behaviours, which this objective does not aim to achieve. This

<sup>55</sup> The fuel tax exemption program is formed by a fuel tax exemption for farm activity, a fuel tax exemption for primary producers of renewable resources, and a tax exemption for fuel used as a heating source.

<sup>56</sup> Provincial Auditor of Saskatchewan, *2016 Report – Volume 1*.

<sup>57</sup> Ibid.

<sup>58</sup> Ibid.

objective is much costlier too, as it accounts for nearly 80 per cent of the total fuel tax exemption program annually.

It can be argued that because the purpose of a gas tax is to help fund the expansion and maintenance of transportation infrastructure, and because farmers consume gas off-road as they work on their fields, then this fuel should not be taxed. However, this is not entirely true. Grain and other agricultural goods in Saskatchewan are moved by roads as grain terminals have been restructured into regional sites. Heavy grain trucks are thus transporting products on local roads and provincial highways. Even though some of this transportation is conducted by commercial truckers, the majority of it is done by farmers themselves. At the same time, the argument for the exemption on heating oil better reflects the true purpose behind tax exemptions as it ensures fairness between different sources of heating fuel.

There are other issues with the fuel tax exemption program, including that fact that its coverage is overly broad. The program only requires a program beneficiary to own or rent 30 hectares for cereal crops or have a minimum gross annual revenue of \$10,000 from the sale of Saskatchewan primary farm products. A member or shareholder in a farm organisation that contributed substantially to its agricultural production can also qualify.<sup>59</sup> These thresholds for eligibility are low because farms in Saskatchewan have grown remarkably in size since 1981. Since more than 94 per cent of farms in Saskatchewan cover at least 52 hectares,<sup>60</sup> almost every farm owner or operator qualifies for the program, and this does not include those with less than 30 hectares but who meet the other eligibility criteria.

This is important because the total fuel tax exemption program represents significant foregone revenue to the government (Table 4). Total (estimated) program costs were \$155.8 million in 2015, plus about \$300,000 in administrative costs. Moreover, total foregone revenue from this program has increased \$22.5 million or 16.9 per cent since 2012. Even though the Ministry recovers approximately \$2.5 million from program participants who self-declare personal fuel consumption, not all beneficiaries make such disclosures.<sup>61</sup> With the continued decline of agriculture's share of Saskatchewan's GDP and employment, it is worth asking if the amounts allotted to this program should continue rising. With the current slump in oil prices worldwide, it is also worth asking if lower oil prices would cut program costs, since farmers presumably pay less for fuel.

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<sup>59</sup> Government of Saskatchewan, *Farm Fuel Program*.

<sup>60</sup> The Conference Board of Canada and Statistics Canada, *Cansim Table 004-0005*.

<sup>61</sup> Provincial Auditor of Saskatchewan, *2016 Report – Volume 1*

Table 4

Calendar Year	Farm Activity	Heating Fuel	Primary Producers	Total Actual (unless otherwise stated)	Total Estimate
2015 (estimate)	121.0	33.1	1.7	155.8	155.8
2014	117.4	31.7	1.7	150.8	145.9
2013	113.6	30.3	1.4	145.3	134.3
2012	104.3	26.8	1.2	132.3	148.3
2011	107.5	26.4	1.3	135.2	141.0
2010	105.3	26.8	1.2	133.3	125.2

Source: Provincial Auditor of Saskatchewan.

**The Fuel Tax Rebate Program**<sup>62,63,64</sup>

*“The farm fuel tax exemption program was introduced before the 1986 provincial election, with the objective of assisting farmers by reducing their input costs.*

*It was stated in the 1987 Fuel Tax Act that a farmer who:*

*(a) on or before December 31st 1992 purchases in bulk diesel fuel intended solely for the use in farming operations from a licensed bulk fuel dealer; and*

*(b) produces a valid fuel tax exemption permit at the time of purchase of the fuel;*

*is exempt from paying the tax with respect to that purchase of fuel.*

*The fuel tax was re-applied to all gasoline purchased by farmers buying from bulk fuel dealers in May 1992. Yet, the Farm Fuel Program allowed for a rebate for tax paid on gasoline and propane used in farming activities. All Saskatchewan primary producers were eligible for assistance under this program. Farmers had to apply annually for this tax rebate on gasoline and propane purchases, and were eligible for a tax rebate of \$0.15 per litre up to a maximum of \$900.00 annually.*

*In 2001, Saskatchewan farmers gained the option of buying their farm gasoline and propane tax-free from bulk fuel dealers. To purchase tax-free fuel from bulk dealers, farmers only needed to use the same permit number used to buy their diesel, marked with a dye, tax-free. Farmers could also buy gas and propane from a retail outlet, but they had to submit their receipts to apply for a tax refund at the end of each year. At that time, Finance Minister Eric Cline stated that changes to the Farm Fuel Program, including the removal of the \$900 annual rebate cap, would leave an*

<sup>62</sup> Government of Saskatchewan, *Farm Fuel Tax Break Takes Effect*.

<sup>63</sup> Government of Saskatchewan, *The Fuel Tax Act 1987* (repealed).

<sup>64</sup> University of Saskatchewan, *Policy Implications of the Saskatchewan Farm Fuel Program and Fuel-Tax Exemptions*.

*additional \$9 million in farmers' pockets. He further said that these changes, combined with other tax exemptions, would save Saskatchewan farmers more than \$270 million a year in input costs.*

*Today, Fuel Tax Exemption Permit holders (farmers, commercial fishers, trappers and loggers) can purchase 80 per cent of their gasoline tax exempt from registered fuel dealers for use in their farming, commercial fishing, trapping or logging activities. Fuel Tax Exemption Permit holders can also purchase marked diesel fuel and propane exempt of tax for use in their eligible farm and primary producing activities. Farmers and renewable resource producers must complete a Farm Fuel Program Permit Renewal each year."*

At the same time, however, it should be noted that industries that are largely located in urban areas also benefit from tax exemptions. For example, recent Saskatchewan budgets have included tax exemptions for the manufacturing industry. Although manufacturing companies have operations across the province and many of them are resource-based, manufacturing activity is still largely centred in urban municipalities, in the same way that agricultural activity is tightly linked to rural municipalities. It is thus fair to view fiscal measures aimed at manufacturing as largely benefitting urban municipalities. The largest tax exemptions found in the provincial budgets are a manufacturing and processing profits tax reduction that cost provincial taxpayers \$15 million in 2015, with another \$15 million budgeted for 2016, along with an investment tax credit for manufacturing and processing that cost \$40 million in 2015, with an additional \$30 million budgeted for 2016.<sup>65</sup> While these pale in comparison with the tax exemptions provided to the agricultural industry, they should nonetheless face equivalent scrutiny. These measures are intended to:

1. Increase investment in Saskatchewan's manufacturing and processing industry; and
2. Provide an incentive for existing firms to stay in the province.<sup>66</sup>

While these tax exemptions may indeed achieve both of these two goals, it is debatable whether manufacturing deserves special treatment compared to other industries across the economy.

Finally, and unfortunately, it is extremely difficult to group the remaining tax exemptions into urban and rural buckets. Rather, these tax measures indiscriminately impact people and firms located in both urban and rural areas. These measures include numerous deductions, credits, and measures designed to reduce the burden of personal income taxes, corporation income taxes, and provincial sales taxes for different groups, regardless of location. These include tax exemptions on children's clothing and reading materials, prescription drugs, basic groceries, construction, and registered pension plan contributions. These measures likely treat residents of urban and rural municipalities equitably, because even though urban centres probably receive the bulk of these exemptions, they also represent a larger share of the population and thus contribute more to the funding of these measures.

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<sup>65</sup> Government of Saskatchewan, *2015-2017 budgets*.

<sup>66</sup> *Ibid.*

## 4.2. Property Taxes

The second type of levy that we examine is the property tax which, by the way they are applied across the province, tend to favour agricultural property at the expense of other property types more likely to be located in urban areas. This is a critical issue for municipalities in the country since the property tax accounts for such a large share of total local government revenue. As previously explained, municipalities in Saskatchewan and across Canada rely heavily on property tax to finance their expenses, which include the high quality level of services and infrastructure that urban residents expect.

Saskatchewan property taxes are generally calculated using this formula:<sup>67</sup>

$$\begin{aligned} \text{Assessment} * \text{Provincial Percentage of Value} &= \text{Taxable Assessment} \\ \text{Taxable Assessment} * \text{Mill Rates} &= \text{Property Taxes} \end{aligned}$$

Properties are first assessed by an assessment service provider. Then, a provincially established percentage of value is applied to obtain the taxable assessment. This percentage of value varies by property class. Finally, municipal and education mill rates are applied to the taxable assessment to obtain the property tax amount. Municipal mill rates are obtained by dividing the amount of taxation revenue required by a municipality (from its budget) by the total taxable assessment in that municipality. Education mill rates are set by the province, and can be found in Table 5. Note that this is a generalised way of calculating property taxes and that many municipalities apply tax tools like a mill rate factor, a minimum tax or a base tax to municipal property taxes, in order to redistribute the cost of providing public services.<sup>68</sup>

By studying different components of the above formula, we can see how agricultural properties get special treatment. First, the percentages of value, which are established by the province, clearly benefit agricultural properties, as shown in Table 6. In fact, with the exception of grain elevators, only between 45 per cent and 55 per cent of the assessed value of range land and other agricultural land properties is taxable, whereas residential and industrial and commercial properties, located in both urban and rural municipalities, are taxable at between 80 per cent and 100 per cent of their value.

At the same time, the education mill rates also favour agricultural properties. The educational mill rate is 1.9 times higher for residential property than it is for agricultural property, and it is 3.1 times higher for commercial and industrial property than it is for agricultural land.

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<sup>67</sup> Saskatchewan Assessment Management Agency, *Understanding Assessment*.

<sup>68</sup> Government of Saskatchewan, *Municipal Property Tax Tools*.

**Table 5 Provincial Education Mill Rates by Property Type**

Municipal Property Type <sup>69</sup>	Education Mill Rate (per cent)
Residential	5.03
Agriculture	2.67
Commercial and industrial	8.28
Resource	11.04

Source: Government of Saskatchewan.

**Table 6 Taxable Percentages of Value by Property Type<sup>70</sup>**

Property Type <sup>71</sup>	Taxable Percentage
Range land and improvements	45
Other agricultural land and improvements	55
Residential	80
Multi-unit residential	80
Seasonal residential	80
Commercial and industrial	100
Grain elevators	100
Railway right of way and pipeline	100

Source: Government of Saskatchewan.

Supporters of lower property tax levies on agricultural properties justify them by pointing out that these land owners must also pay property taxes on their residences. Indeed, the lines between residential and agricultural property can be blurry in rural municipalities, as farmers tend to live where they work.

Some may also argue that urban and rural residents benefit by an equivalent amount from lower residential percentages of value and lower residential educational mill rates, compared to commercial, industrial, and resource-based properties. But this is not true. Residents of rural municipalities can reduce

<sup>69</sup> Government of Saskatchewan, *No Education Mill Rate Increase in 2016*.

<sup>70</sup> Includes expected changes to percentages of value for 2017.

<sup>71</sup> Saskatchewan Assessment Management Agency, *How Property Assessment Works in Saskatchewan*.



all or a portion of the taxable assessment on their principal dwelling by writing off the total taxable assessment on their agricultural land.<sup>72</sup>

Putting all of this together, agricultural land owners, residents of rural areas, receive the following benefits that are partly or wholly unavailable to residents of urban areas:

1. Reduced assessment of their properties thanks to the provincial percentages of value; only 45 per cent of the value of range land can be taxed, only 55 per cent of the value of other agricultural land can be taxed, only 80 per cent of the value of residences can be taxed;
2. Reduced residential taxable assessments by writing off the value of the taxable assessment of owned or rented agricultural land, and;
3. Lower education mill rates on their agricultural property.

As mentioned above, it is important to note that despite these advantages in the treatment of property taxes, each municipality can use tools at its disposal to redistribute the burden of the tax. Consequently, the above findings do not necessarily mean that all rural residents pay lower effective property tax than do urban residents. However, it is clear that current provincial property tax policies (percentages of value and education mill rates) advantage farmers.

### 4.3. Municipal Revenue Sharing<sup>73</sup>

Municipal revenue sharing (MRS), a provincial government commitment to distribute one full percentage point of the 5 per cent provincial sales Tax (PST) to municipalities every year, benefits all municipalities in Saskatchewan. The MRS program is the largest direct source of provincial funding to municipalities<sup>74</sup> and a key municipal budget support. Moreover, given that revenues generated from sales taxes tend to grow with the economy, funding from this program has increased strongly since the inception of its current formula in 2011-12, rising from \$167 million to a projected \$271 million in 2016-17, a 62.3 per cent rise.<sup>75</sup>

Figure 10 shows the geographic allocation of this funding. In 2011-12, urban municipalities<sup>76</sup> received 64 per cent of the total grant, rural municipalities received 29 per cent, and northern communities received 7 per cent. For 2016-17, the distribution of the MRS was 64.3 per cent for urban municipalities, 28.3 per cent for rural municipalities, and 7.5 per cent for northern communities.

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<sup>72</sup> Government of Saskatchewan, *The Municipalities Act*.

<sup>73</sup> All amounts in this section are budgeted amounts.

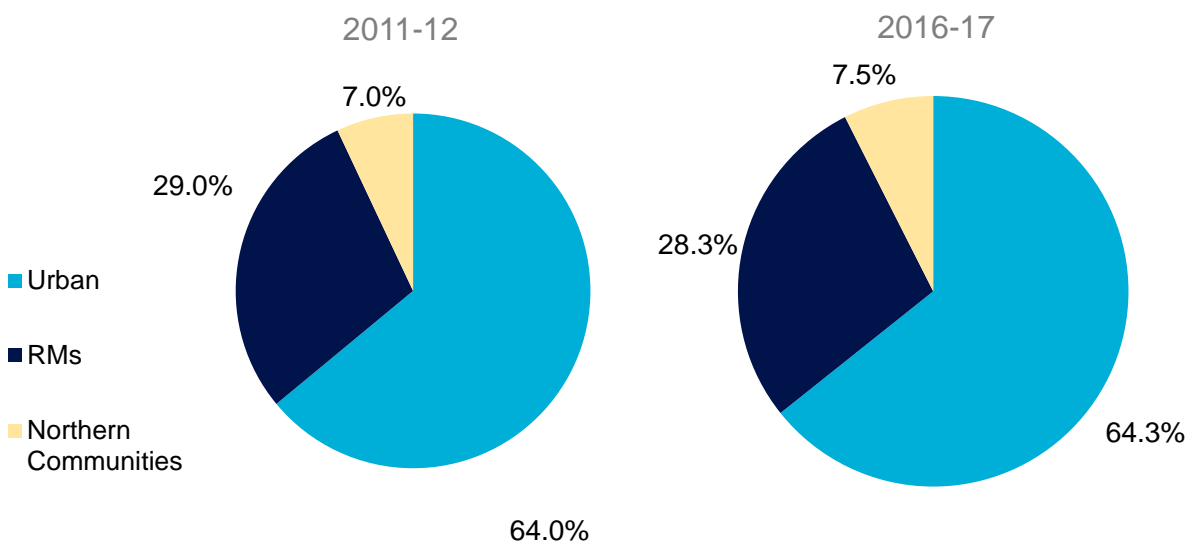
<sup>74</sup> Government of Saskatchewan, *2015-16 Budget Provides Record Municipal Revenue Sharing*.

<sup>75</sup> Government of Saskatchewan, *Municipal Revenue Sharing*.

<sup>76</sup> Although the MRS allocation for cities, towns, villages, and resort villages varies, we have averaged them together into allocation for urban municipalities.

Figure 10

### Municipal Revenue Sharing



Source: Government of Saskatchewan and The Conference Board of Canada.

Even though the share of MRS revenue granted to urban municipalities has only increased by 0.3 percentage points since 2011-12, its share of the population has continued to increase, albeit gradually. In 2011, 76 per cent of Saskatchewan’s population was urban. This ratio edged up to 77 per cent in 2016. As for rural municipalities, their share of MRS has decreased by 0.7 percentage points over the same period, but their share of the population has decreased a touch faster, falling from 17 per cent in 2011 to 16 per cent in 2016. In other words, urban municipalities currently receive a below per capita share of MRS funding, while rural municipalities receive a share of MRS above their share of population, a situation that has not changed since 2011-2012. Thus, the allocation of the funding is not in line with Saskatchewan’s demographics, just like the tax exemption programs and the property tax regime.

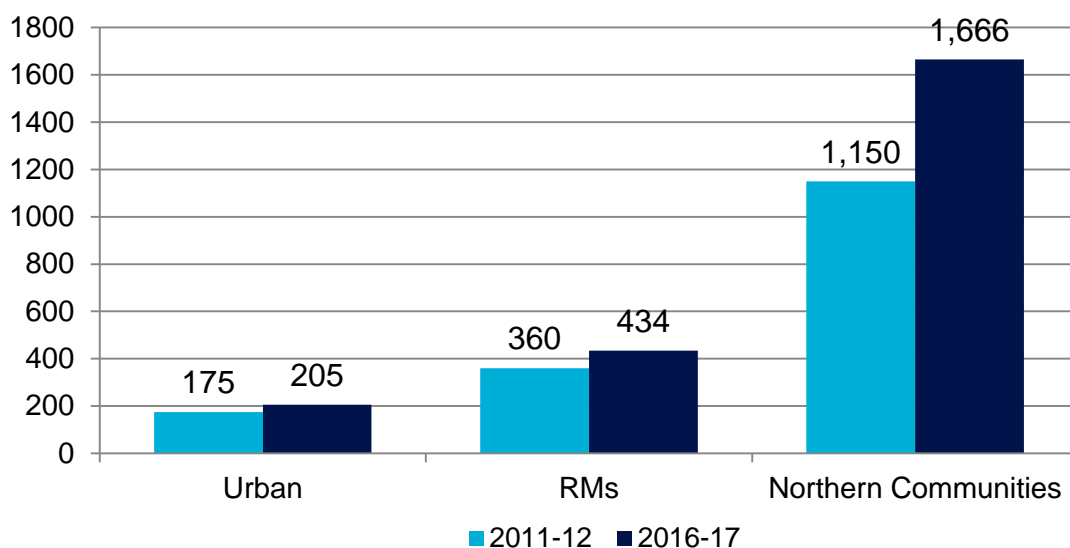
Indeed, rural municipalities receive much more MRS program funding in per capita terms than do urban municipalities. Based on 2016 census data, rural municipalities will receive an average of \$434 per person in 2016-17, while urban municipalities will receive, on average, just \$205 per person. (See Figure 11). In other words, per capita funding for urban municipalities through the MRS program is less than half of that for rural municipalities. Since 2011-12, the average per capita amounts received by urban municipalities have increased by approximately \$30, while the amounts received by rural municipalities have increased by \$74.

It also should be noted that some have argued that rural municipalities have seen their share of MRS funding decrease sharply since 2007-09. Indeed, their share of MRS funding stood at 40 per cent in that fiscal year, but now their share is below 29 per cent. However, this dramatic decrease is the result of a change to the MRS funding program when the province transferred conditional road and bridge funding

and primary weight corridor funding —funding aimed at building and maintaining rural roads and bridges, as well as roads facing heavy traffic from industry— to the Ministry of Highways and Infrastructure starting in 2009-10. As a result, rural municipalities still receive this funding, albeit not through the MRS program. The share of MRS funding received by rural municipalities has remained stable since this transfer in 2009-10, even once the formula was updated in 2011-12.<sup>77</sup>

**Figure 11**

**Municipal Revenue Sharing**  
(dollars per capita)



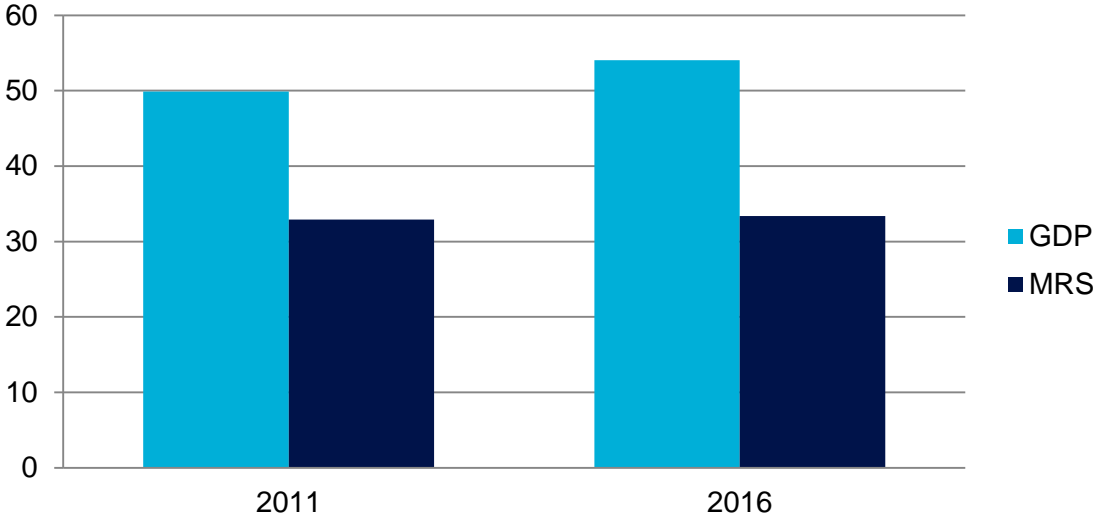
Source: Government of Saskatchewan, The Conference Board of Canada, Statistics Canada.

Additionally, we can also use GDP shares as another means of comparison. In fact, rural municipalities have argued that GDP contribution is a better measure than a per capita allocation, because natural resource extraction plays such a key role in the province’s economy. Unfortunately, it is difficult to accurately allocate proportions of provincial GDP to urban and rural municipalities, so we employ only Conference Board estimates of GDP for Regina and Saskatoon. Figure 12 illustrates that together, Regina and Saskatoon represented 49.9 per cent of Saskatchewan’s GDP and 32.9 per cent of the MRS in 2011. In 2016, Regina and Saskatoon are expected to make up 54 per cent of GDP, an increase of 4.1 per cent. However, their share of MRS will be about 33.4 per cent, a 0.5 increase. Thus, even when using GDP to scale MRS funding, Regina and Saskatoon do not appear to be getting their fair share.

Put together, it is clear that the MRS funding program favours rural municipalities over urban ones, given the disparity in per capita and GDP allocations. This is on top of already special treatment through tax exemptions and property tax regulations. We will return to this topic in the concluding chapter when we detail our recommendations.

<sup>77</sup> The Conference Board of Canada and Government of Saskatchewan, *Municipal Revenue Sharing*.

**Figure 11**  
**Regina & Saskatoon Shares of Provincial GDP and MRS**  
(per cent)



Source: Government of Saskatchewan, The Conference Board of Canada.

## 5. Key Issues and Pressure Points

### Chapter Summary

- The commodities boom that ran until late 2014 drew thousands of people to Saskatchewan's urban municipalities.
- The rapid population growth of these areas has increased fiscal pressures for local governments.
- Urban local governments and urban citizens receive fiscal help from the province in the form of MRS funding, tax exemptions, and other programs. However, more is required if these urban areas are to remain competitive in attracting firms and individuals.
- Rural municipalities' depopulation comes with its own set of issues. Most notably, it is more difficult to fund maintenance and expansion of the transportation network, vital to Saskatchewan's economy.
- However, rural local governments and rural citizens appear to be receiving sufficient funding to tackle their most pressing issues.

This chapter uses the findings and conclusions drawn in previous sections to summarize the key issues and pressure points for urban and rural municipalities in Saskatchewan. The demographic and economic analysis conducted so far helps us understand the fiscal requirements for municipalities in the province and the potential threats to continued and sustainable growth. The analysis described in Chapter 4 gives us a sense of which fiscal regimes and programs should be updated to better reflect the current demographic and economic trends in Saskatchewan.

Urban municipalities face fiscal capacity constraints to fund spending on infrastructure and services, as their populations' grow rapidly. Rural municipalities face a different issue: they are tasked with maintaining their share of the transportation network, vital to moving Saskatchewan's goods to domestic and international markets, while their populations dwindle. Even though urban and rural municipalities can count on an array of tools and programs aimed at alleviating their respective fiscal burdens, rural governments appear to be in a strong position to face their most pressing issues while urban governments require additional measures to keep up with their current challenges.

### 5.1. Urban Governments

Saskatchewan has enjoyed rapid population growth in recent years, although most of it has been concentrated in urban centres. For instance, Saskatchewan's population increased by 1.3 per cent per year from 2006 to 2016. In Regina and Saskatoon, the growth rates were 1.8 per cent and 2.0 per cent, respectively. In the 2011 Census, 76 per cent of the province's population was urban, while in 2016 this share hit 77 per cent.<sup>78</sup>

A booming economy and strong job growth drew thousands of people into Saskatchewan's urban centres from other parts of the province, other parts of Canada, and from other parts of the world. True, the economic strength stemmed largely from a surge in demand for commodities, and resources are largely

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<sup>78</sup> The Conference Board of Canada and Government of Saskatchewan, *Saskatchewan Census Population*.

extracted outside of urban areas. However, urban-oriented industries, like manufacturing and many services sectors, also benefitted from the commodities boom. But this strong growth also comes at a cost for local governments—strong population gains increase the demand for services and infrastructure provided by urban municipalities, leading to intensified fiscal pressure.

Although the end of the commodities boom has led to much weaker economic conditions over the past two years, population gains have remained decent. But regardless of current underlying trends, if Saskatchewan’s urban municipalities are going to remain attractive to both people and business investment, they will need to continue to provide a high level of quality of services and infrastructure. The current fiscal arrangement makes it very difficult for them to meet these needs.

Certainly, it is undeniable that when populations soar urban governments must increase police, firefighting, sanitation, housing, transit, and cultural and recreational services. Urban governments must also incur the maintenance costs of increased usage of municipal infrastructure, like roads and water mains. Additionally, it is not unusual for rural residents residing close to urban municipalities to access some urban services and infrastructure, further increasing their use. This helps push urban governments’ expenditures up faster than revenues. This is because the cost of services is mostly supported by property tax revenues—the main revenue source for municipalities—but they don’t necessarily grow with the economy like other types of taxes.

True, urban local governments also receive funding through their share of MRS payments, which helps to offset some of the shortfalls of the property tax system. At the same time, governments have access to additional funds through the Urban Highway Connector Program and parks, recreation, and culture grants.

Additionally, some firms and residents located in urban areas also receive government support. For instance, manufacturing and processing (M&P) companies, which tend to cluster in urban centres, receive special tax exemptions and investment tax credits. Urban residents receive their fair share of province-wide tax exemptions, like those for construction, children’s clothing and reading materials, prescription drugs, and basic groceries.

Although urban governments might be able to raise additional funds by increasing property taxes on industrial and commercial buildings, this could drive firms away. Firms in urban centres tend to be more mobile, since firms in rural areas are often closely tied to mineral deposits or crop fields. Similarly, local governments could also raise property taxes on residential property, but as we argue earlier in the report, the link between assessed property value and ability to pay is not often closely linked.

### 5.2. Rural Governments

At the other end of the spectrum, the depopulation of rural Saskatchewan presents its own set of issues for the province’s rural municipalities. In fact, the rural population<sup>79</sup> declined from 240,472 in 1981 to 176,535 in 2016, a decrease of 27 per cent over 35 years.<sup>80</sup> Although this eases the pressure of providing

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<sup>79</sup> Excluding Indian reserves, northern hamlets and villages, and unorganized territories.

<sup>80</sup> Government of Saskatchewan, *Saskatchewan Census Population*.

services to the local population, these rural governments are still partly responsible for expanding and maintaining their transportation infrastructure, which is vital to moving the province's natural resources and agriculture products. As mentioned earlier in the report, exports of natural resources and agricultural output drive Saskatchewan's exports in the province, suggesting that rural governments have a legitimate claim on some level of provincial and industry support for construction and maintenance of the transportation network. Indeed, such spending accounts for the bulk of rural government expenditures.<sup>81</sup>

However, not all is grim in rural Saskatchewan. Despite agriculture's decreased weight in the province's economy, farmers are faring increasingly well. The province's average farm size has been increasing rapidly and the average financial situation of Saskatchewan farmers has been generally improving. Farmers' welfare should continue to benefit from advances in technology that make previous agricultural uncertainties more manageable. Data satellites, Global Information Systems (GIS), and Global Positioning Systems (GPS) are already being used to forecast yields, to follow changes in soil conditions, and to automate agricultural equipment. A resulting ability to tailor farming practices reduces risks, produces better yields, and lower input costs.<sup>82</sup>

Moreover, as our report has shown, rural municipalities currently enjoy measures that alleviate their fiscal burden. Rural governments receive a much higher per capita level of MRS program funding compared to their urban counterparts. In 2014, revenue from the MRS grant and from the industrial property tax levy covered about 77 per cent of rural governments' transportation expenditures.<sup>83,84</sup> Furthermore, these governments also get funds allocated through the Municipal Roads for the Economy Program. Putting all these programs together, it appears that rural governments receive enough support from industry and government to adequately build and maintain the transportation network to support the energy and mineral extraction sites located in their jurisdictions.

All in all, rural governments appear to have the necessary support from the provincial government to keep up with their most pressing issues, but the same claim cannot be made about Saskatchewan's urban governments. We will offer recommendations to address the imbalance of support between urban and rural municipalities in the report's conclusion, which is where we turn to next.

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<sup>81</sup> Criton, *2014 Municipal Financial Information*.

<sup>82</sup> Alberta Agriculture and Forestry, *What is Precision Farming?*

<sup>83</sup> The Conference Board of Canada and Government of Saskatchewan, *Municipal Revenue Sharing*.

<sup>84</sup> Criton, *2014 Municipal Financial Information*.

## 6. Conclusion and Recommendations

### Chapter Summary

- The provincial government's call for transformational change presents an opportunity to reassess the fiscal policy framework. We recommend that any changes made be in line with the current economic and demographic situation in Saskatchewan.
- We recommend that urban municipalities be empowered with greater fiscal tools, particularly increased control to raise their own revenue.
- We recommend that urban municipalities' share of MRS funding be increased, reducing the current per capita and GDP gap between urban and rural allotments. The fairest and least controversial approach would be to increase transfers to urban municipalities while keeping rural municipalities and northern communities funding levels constant.

The current fiscal situation in Saskatchewan is obviously difficult. The province's economy is at the tail-end of a significant slowdown, hit hard by a sharp decline in commodity prices. This sent the province into a recession in 2015, which has persisted into 2016. As a result, royalty revenues – which made up 19 per cent of total revenues in 2014–15 at \$2.6 billion – are expected to be half their value, at \$1.3 billion, just two years later. Accordingly, the government has been forced to revise its estimate for the fiscal year (announced in a mid-year update) downwards – bringing the deficit estimate to just over \$1 billion (before pension adjustments).

Given this large deficit, difficult decisions will have to be made for the provincial government to balance its books. But, at the same time, it also presents an opportunity to reassess and revise the current fiscal policy framework. Indeed, this is the motivation behind the provincial government's call for “transformational change.”

Whatever reforms are chosen, they should be done in the context of Saskatchewan's changing economic and demographic structure. The reforms should also be in full alignment with the Saskatchewan Plan for Growth<sup>85</sup>; i.e., they should help the province's economy to better adapt and prepare for challenges as well as to promote opportunities for growth and diversification.

In particular, reforms should be carried out under the understanding that the province's cities account for a large and growing share of total economic activity, and this trend is expected to continue over the coming years. As discussed throughout this briefing, Saskatchewan's economy is becoming more services-oriented, which in turn, is increasing the importance of urban centres as drivers of economic growth. True, the provincial economy continues to benefit from the rural-oriented natural resource sector, but many value-added activities to resources take place in larger urban areas. In fact, the future success of the province's resources industries depends upon the skilled workers who overwhelmingly reside in urban municipalities.

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<sup>85</sup> Government of Saskatchewan, *Saskatchewan Plan for Growth: Vision 2020 and Beyond*.



But in order to attract and retain these skilled workers, many of whom will be immigrants, the province's urban centres will need to offer not only meaningful job prospects, but also a high quality of life. Indeed, such sought-after individuals are attracted to urban areas that provide high-quality services and infrastructure, both of which require these municipalities to have the fiscal capacity to fund programs and to finance capital spending.

With this in mind, the Conference Board of Canada makes two recommendations for fiscal policy reform. These recommendations are based on certain core principles, namely that fiscal measures should aim to increase fairness, serve an economic or social goal, or encourage targeted behaviours.

### **A. Empower Urban Municipalities with Greater Fiscal Tools**

Saskatchewan's engine of growth has been, and will continue to be, urban municipalities. But this strong economic and population growth is also putting a burden on local governments, as the current fiscal arrangement in which property taxes are the dominant revenue source is constraining their ability to keep up with rapidly growing demand for municipal services and infrastructure. Thus, the Conference Board argues that urban municipalities should be granted access to more revenue options. Greater political autonomy and increased control over revenue-raising and expenditures will give urban areas the tools required to succeed. The provincial government should design new approaches to municipal funding in order to allow for a strategic allocation of funds that is in line with the distinct needs and potential of municipalities. Such an approach could include giving municipalities access to additional sources of revenue such as new taxes and user fees. Allowing municipalities to levy more user fees would help achieve the objective, whenever possible and desirable, of charging for public services rather than giving them away, thus making government's use of resources more efficient.

At the same time, the Conference Board also recognizes that better urban governance is also a necessary condition for building more vibrant and prosperous municipalities. Municipal governments should undertake cross-municipality research into public service delivery costs and spending, with the aim of setting benchmarks and assessing the cost-savings potentials and pitfalls of competitive service delivery models. Municipal governments should also be less reluctant to move from general taxation to user fees.

Finally, the provincial government may be tempted to cut back on infrastructure spending, as a way to improve their fiscal situation. However, we recommend against this approach. Research has found a strong correlation between the physical stock of public capital and an economy's overall labour productivity, so cutting back on infrastructure investment could prove to be counterproductive. There is indeed a high degree of interdependence between the quality and quantity of public infrastructure, the performance of a society's business sector, and, ultimately, the quality of life of its citizens. Infrastructure construction spending is also useful in countering the business cycle over the short term, and the completed infrastructure projects can lead to productivity gains over the medium and the long term.

### **B. Increase Urban Municipalities' Share of MRS Funding**

The inception of the Municipal Revenue Sharing program shows that the provincial government recognizes the importance of municipalities, both urban and rural, as sources of economic growth in Saskatchewan. The MRS program gives municipalities access to revenue that is more likely to grow with

the economy, unlike the property tax. However, the program is not perfect. As shown in Chapter 4, there is a significant per capita and GDP imbalance between the amounts allotted to urban and rural municipalities. In fact, rural municipalities receive almost twice as much funding as urban municipalities in per capita terms. In terms of GDP, Regina and Saskatoon not only receive a share of MRS below their share of provincial GDP, but their share of GDP has grown faster than their share of MRS in the last five years.

The Conference Board recommends that the province consider a more balanced allocation of MRS funds between rural and urban municipalities. The fairest and least controversial approach would be to increase MRS transfers to urban municipalities, while keeping RMs and Northern Communities' funding levels constant.

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