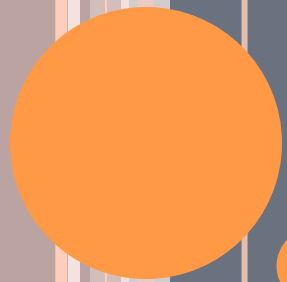


**DISCUSSANT COMMENTS FOR: “GOOD  
HOUSEKEEPING: THE PROVINCIAL  
IMPOSITION OF A HARD BUDGET  
CONSTRAINT ON ONTARIO  
MUNICIPALITIES IN THE GREAT  
DEPRESSION” BY A.T. TASSONYI**

**Comments Prepared by L. Di Matteo for the  
2012 Canadian Economics Association  
Meetings, Calgary**



# SUMMARY OF PAPER

# SUMMARY-I

- This paper is in the tradition of the “New” fiscal federalism
- Shift from the “fiscal federalism” model of an all powerful national or federal government in the first generation (FGT) literature to the “federal finance” model of powerful sub-national governments.
- The concept of “good housekeeping” comes from the literature on the gold standard and sovereign borrowing as a different form of constraint.



## SUMMARY-II

- Governments in Canada have maintained fiscal health in part due to lessons of Great Depression
- Ontario in 1930s – imposed a long-lasting hard budget constraint on Ontario municipalities
- This supervision improved the fiscal circumstances of Ontario municipalities – may have been perceived by creditors as an implicit guarantee of municipal debts



## IMPLICATION

- *“...both market and hierarchical constraints operate in the Canadian context and have seemingly prevented crises in sub-national finance since the Great Depression. It is not clear that continuing to impose the 1930s straight jacket on municipalities is warranted.”*



## COMMENTS

- This is timely given the sovereign debt issue facing international economies. [If only Mitch Hepburn had been in charge of Greece]
- Indeed, as Tassonyi writes: “The circumstances of small debtor countries under the gold standard in the late nineteenth century and the circumstances of Ontario municipalities in the early twentieth century were somewhat similar. Both groups were price-takers in the capital market and had little independence in terms of monetary policy...”



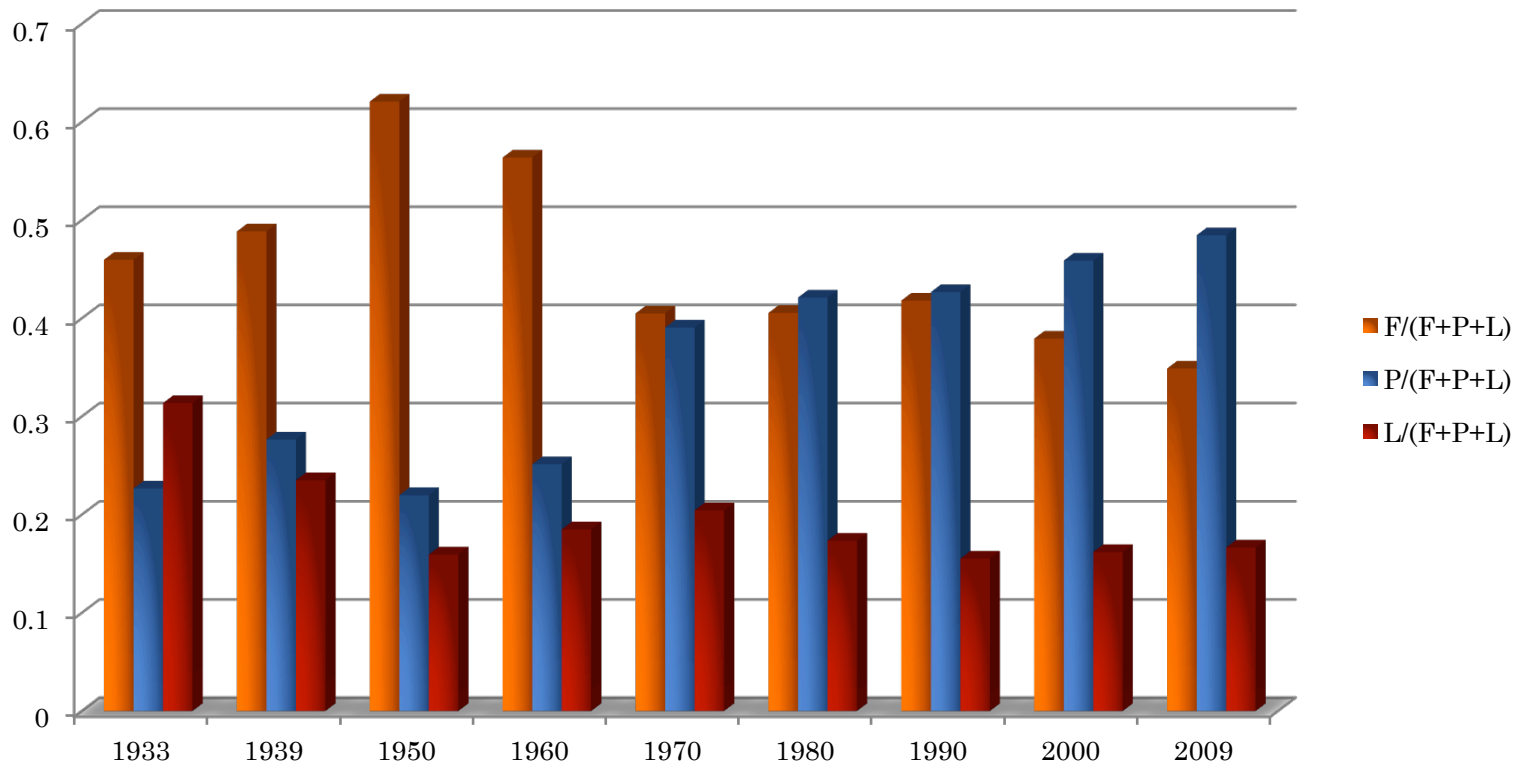
## HOWEVER...

- Ontario municipalities have always had their sovereignty at the discretion of the province – “creatures of the province” according to the BNA
- Financial crisis of the 1930s for Ontario municipalities was a provincial responsibility to deal with. It was also a fiscal opportunity for the province [and ultimately all provinces and their municipalities] that strengthened provincial power.



*UNTIL THE 1930S, MUNICIPALITIES WERE ACTUALLY MORE IMPORTANT THAN THE PROVINCES IN EXPENDITURE TERMS...*

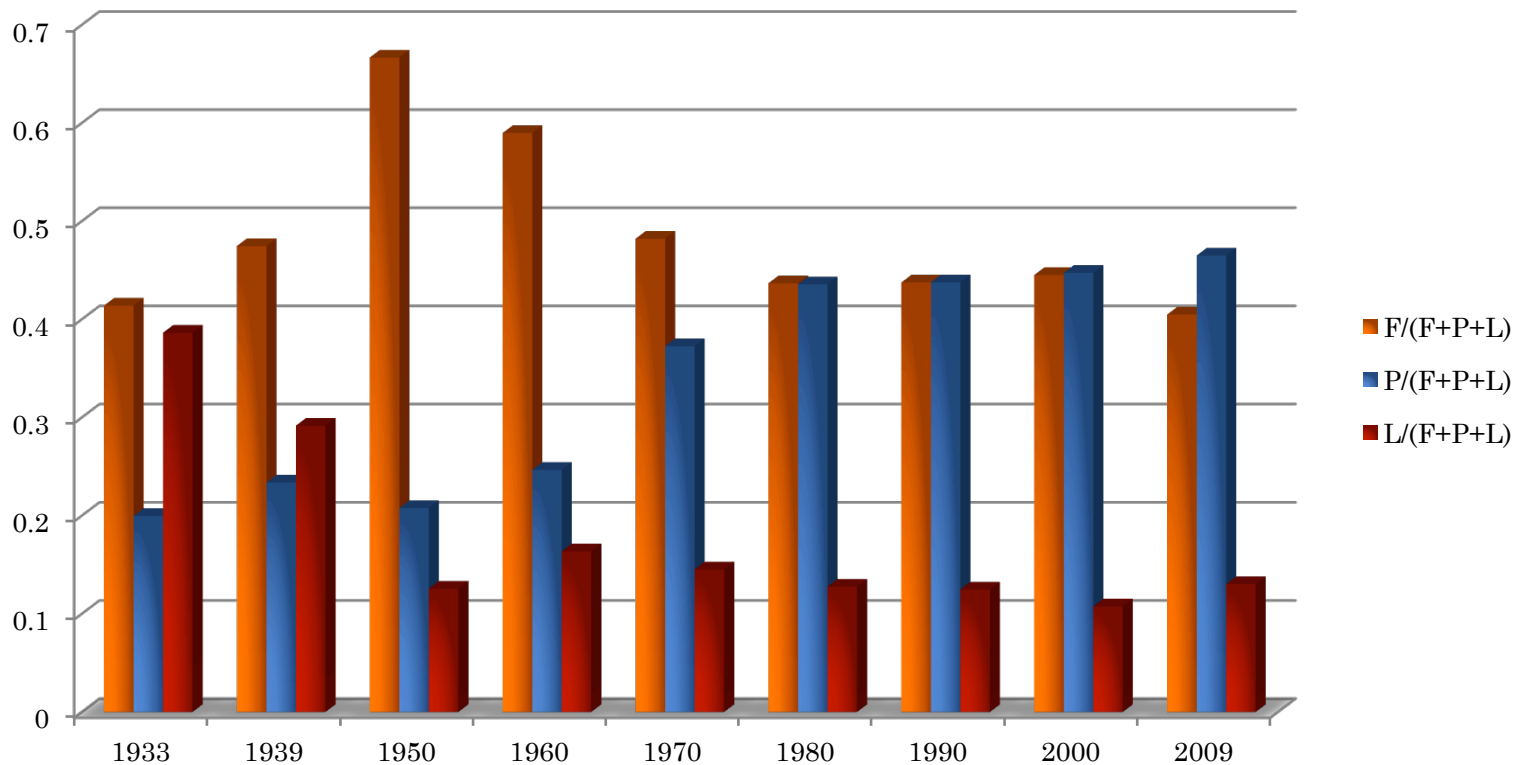
**Expenditure Shares By Fiscal Tier (Including Transfers): Canada 1933-2009 (Data source: HSC & Fed Fisc Ref Tables)**





*MUNICIPALITIES WERE EVEN MORE IMPORTANT WHEN IT CAME TO REVENUE SHARES...*

**Own Source Revenue Shares By Fiscal Tier,  
Canada 1933-2009 (Data source: HSC & Fed Fisc  
Ref Tables)**

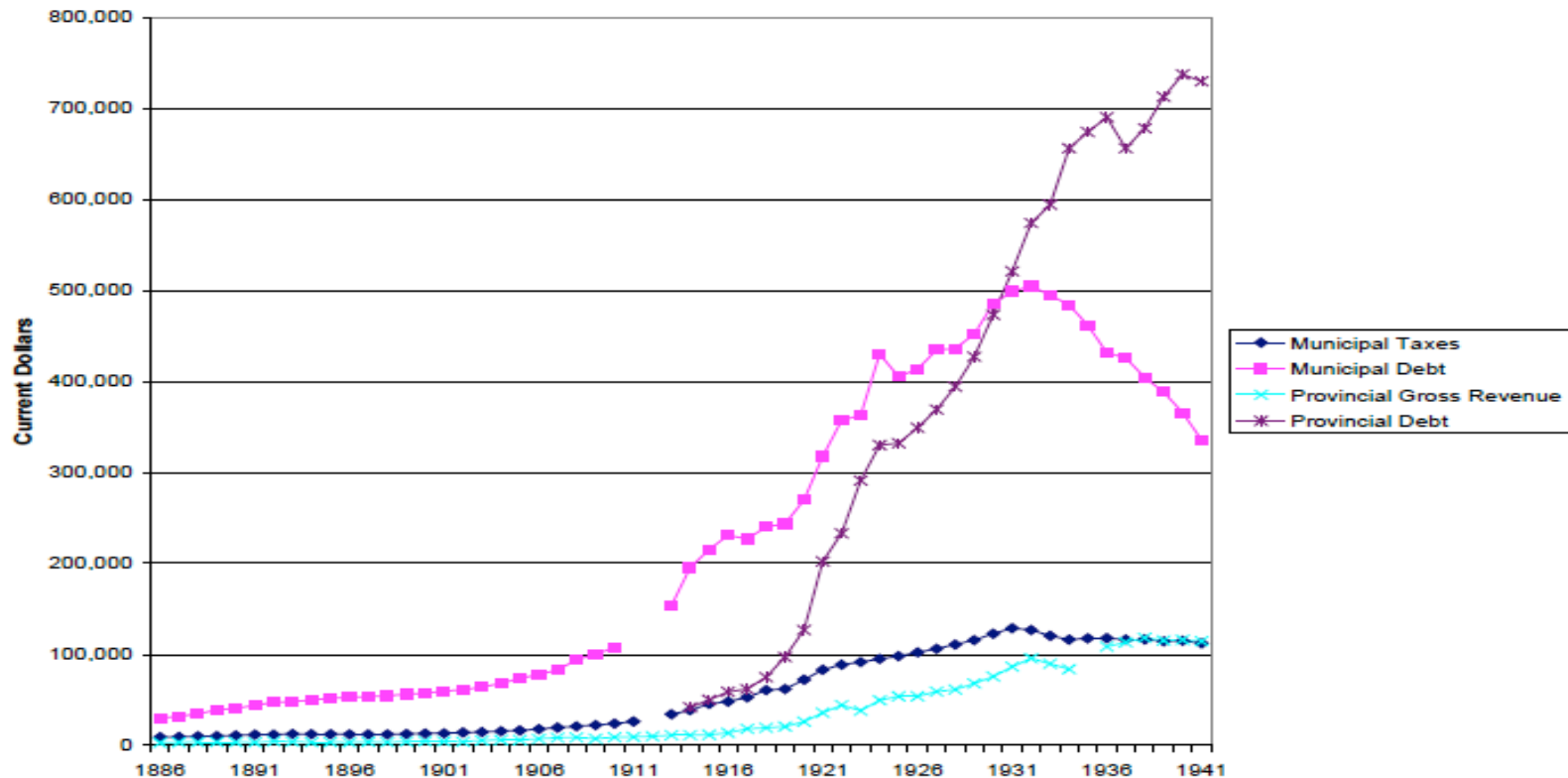


# PROVINCES ARE NOW THE DOMINANT FISCAL TIER

- How did this happen?
- The first steps were taken in the 1930s
- While municipalities were “creatures of the provinces”, they were politically difficult to attack given the grass-roots nature of their services.
- Ontario led the way...
- The catalyst was the municipal debt crisis.



## *PROVINCIAL-MUNICIPAL COMPARISONS OF TAXES & DEBT – ONTARIO 1886-1941 (SOURCE: TASSONYI FIGURE 1)*



Source: Annual Reports of the Ontario Bureau of Industries, the Department of Municipal Affairs and Drummond (1980).

# GREAT DEPRESSION

- Financial stress – by 1934, 40 Ontario municipalities had defaulted. Rising debt and collapse in property taxes.
- Municipal debt was greater than province's but province's was rising faster.
- Municipal revenues were still greater than province's revenues
- Province was liable for debt at both levels both - hard budget constraint an “opportunity”



# IMPACT OF HEPBURN SOLUTION

- Imposition of supervision and hard budget constraint did improve the financial position of municipalities as Tassonyi notes.
- Yet, as Tassonyi notes: “It is not clear that the maintenance of the hard constraint on municipalities is warranted.”
- Why does the hard constraint persist?



# IT WAS NOT ABOUT THE MONEY...IT WAS ABOUT POWER!

- Remember the famous line by Al Pacino as Tony Montana in Scarface?
  - *“In this country, first you get the money, then you get the power, THEN you get the woman.”*

For Ontario, it was of course about the money and the power. Curbing municipal power and placing them under the closer control of the province was the opportunity afforded by the debt crisis.



# PROVINCIAL OVER-REACTION?

- Creation of Ontario Municipal board for approval of debt issue and balanced budgets on operating budgets – created provincial room for easing their own debt and fiscal problems.
- In long run, fiscal restrictions on municipalities and the greater tax bases of the province(s) allowed them to grow and become the dominant fiscal tier.



# PROVINCIAL EVOLUTION

- During the 1930s, the provinces tackled the municipalities.
- Since the 1970s, the provinces have tackled the federal government.
- The provinces have now become the dominant fiscal tier.
- In part, Ontario's pursuit of the "hard budget constraint" for its municipalities is part of the story of how the provinces have grown to become the dominant fiscal tier.





# FEDERAL ROLE?

- The federal government was unwittingly complicit in the demise of the municipal role by its position that unemployment relief and assistance were provincial/local responsibilities. It helped generate the municipal fiscal crisis.
- In the end, the counterbalance to provincial power of strong municipalities was lost leaving the federal government open to provincial assaults...

