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Innovative Financing for Transport Schemes:
A European reference resource

Briefing Paper 6
Public Levies -
Sales Tax Increase Financing
September 2015


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Sustainable transport for North-West Europe's periphery

Sintropher is a five-year €23m transnational cooperation project with the aim of enhancing local and regional transport provision to, from and withing five peripheral regions in North-West Europe.

INTERREG IVB

Investing in Opportunities

This project has received European Regional Development Funding through INTERREG IV B.

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INTERREG IVB

INTERREG IVB North-West Europe is a financial instrument of the European Union's Cohesion Policy. It funds projects which support transnational cooperation.

Working in association with the POLIS European transport network, who are kindly hosting these briefing papers on their website.

Report produced by University College London

Lead Partner of Sintropher project

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Background

This briefing paper is one of a series that together comprise a European reference resource for innovative approaches to financing transport schemes (capital costs) with particular reference to light rail and tram-based schemes in cities and regions. The approaches are also relevant to capital financing of transport schemes generally.

The resource is one of the Investments undertaken for the Sintropher project funded under the INTERREG IVB North West Europe Programme for transnational co-operation. The overall aim of Sintropher project is to develop sustainable, cost-effective solutions to improve connectivity to, from and within poorly connected regions in North-West Europe - to use innovative transport links to connect peripheral regions of NWE with the core European transport network of high-speed trains, via effective interchange hubs.

There has been a particular focus on tram-train systems which allow local trams to run on to national rail networks, pioneered in Germany, firstly in Karlsruhe and developed in Kassel, which allow urban tram systems to extend over national rail tracks to serve extensive city regions. The project has also looked at other innovative forms of tram systems such as single-track tramways, as well as high-quality transport interchanges that link such systems to major national or transnational rail or air hubs.

The project began in late 2009, with fourteen partner agencies in five EU Member States, and lead partner University College London (UCL): Valenciennes (France); the Fylde Coast (UK); West Flanders (Belgium); North Hesse (Germany); and Arnhem-Nijmegen (Netherlands).Participants included public transport operators, local authorities, regional transport agencies, and universities.

They have worked together on a series of feasibility evaluations, pilot investments and demonstration projects, as well as comparative analyses of EU best practice. The total budget is more than €23m, with funding part-financed by the EU's INTERREG IVB Programme.

A €1.5m project extension in 2014, covers follow-on work to capitalise on results from the initial project, and added a fifth objective: to test technologies for low cost transport links in different territorial contexts, plus integrated territorial corridor plans that help these links unlock wider economic and regeneration benefits; and better recognise these in business cases. This included two new partners (total now 16) and two extra demonstration regions (total now 7) in West Flanders Brugge-Zeebrugge (Belgium) and Saar-Moselle (a cross-border region France-Germany).

Innovative financing for transport schemes - increasingly important

Results in the European demonstration regions, plus topics at Sintropher Conferences and Workshops indicate that new tram-based or tram-train proposals are usually technically feasible and can often offer a reasonably positive investment case - especially if the case goes wider than conventional cost-benefit analysis (CBA) to include realisation of territorial objectives and benefits, such as economic growth and social opportunities.

But implementation can be impeded by lack of available funding due to cuts in public expenditure following the European economic crisis of 2008 and subsequent recovery efforts by national governments. Regions that are weaker in population or economic terms have even more difficulty in justifying an investment case in terms of public expenditure, so innovative financing is of growing importance - and much can be learned from approaches in different European countries.

Sales Tax Increase Financing

Taxes have always been used to fund public spending. However, in recent years new tax-based funding schemes have been created in order to provide large funding inputs for particular projects and necessary public expenditures. Fuel taxes on petrol or diesel have been a popular choice, in which the funds from the sales tax imposed is used to finance public infrastructure improvements. Alternatively, taxes on goods are used to regulate and discourage usage of the goods in question.

In recent years, the concept of taxing goods has expanded in order to fund major infrastructure investments. This has resulted in Sales Tax Increase Financing, and is used as a blanket tax increase to generate large funding opportunities. The difference in the newly increased tax rate and the old is then put towards public transport, road upgrades, or any other public infrastructure initiative that is required, based on the needs of the existing government and authorities.

Financial Mechanism

Sales Tax Increase Financing is a mechanism used to gain large quantities of funding for large transport investments. A one-time tax increase is added to the current sales tax of the region, and the funding from that increase is available for use in transport projects and initiatives.

A blanket sales tax increase is imposed, covering applicable goods and services sold (as determined by the government). The tax increase funds are transferred into the government coffers along with the regular sales tax, by means of a yearly sales tax return during the tax accounting season. The funding from the increase in tax is pooled into a pot that is designated specifically for public realm investments as dictated by the original proposal from the sales tax increase. This helps to funds the public endeavours of the government.

Attractiveness

- New investments will go mainly to transit improvements, which benefit lower-income people in particular (since they rely more on public transit). As a result, the proposal is likely progressive overall
- Given the political will (and enough pressure), the provincial government could off-set any negative impact by increasing the PST credit for lower-income people, boosting the low-income carbon tax credit, or extending the discount U-pass to lower-income people
- General horizontal equality

Risks

- Regressive impact on lower-income households due to increase in overall taxes; if not addressed by government tax cuts or other methods of tax equality, lower-income salaries would be more affected by the tax increase
- General vertical inequality between salary levels
- Difficult to justify to car lobby why a blanket tax mechanism should be used, versus targeting users of public transit
- If large enough, the tax increase can impact public spending on goods and services, impacting the local and regional economy
- Without a political champion or strong political will, a referendum could take place to poll the public about whether to implement the tax. In many North American regions, the public will react poorly to increasing taxes for the benefit of a service that they will not necessarily use (due to high car ownership in North America)

Track Record

Sales taxes are popular in North America, and less common in European countries. In the US, after federal funds, sales taxes comprised the largest source of revenues for capital spending (38%) and the second largest source of operating expenses (27%) after fares (32%). In 2008, more than two-thirds of Los Angeles County voters approved Measure R, a referendum that established a special 0.5% sales tax dedicated to rapid transit and some road infrastructure.

Generally, sales taxes have seen mixed results, with public referendums either passing or failing the initiative.

Sales Tax Case Study: Vancouver, Canada

Financial Specifications

Amount(s)

0.5% increase on provincial sales tax within Metro Vancouver

Targeted Groups

All tax payers within the set region

Timeline

Originally presented to public in 2015: Failed

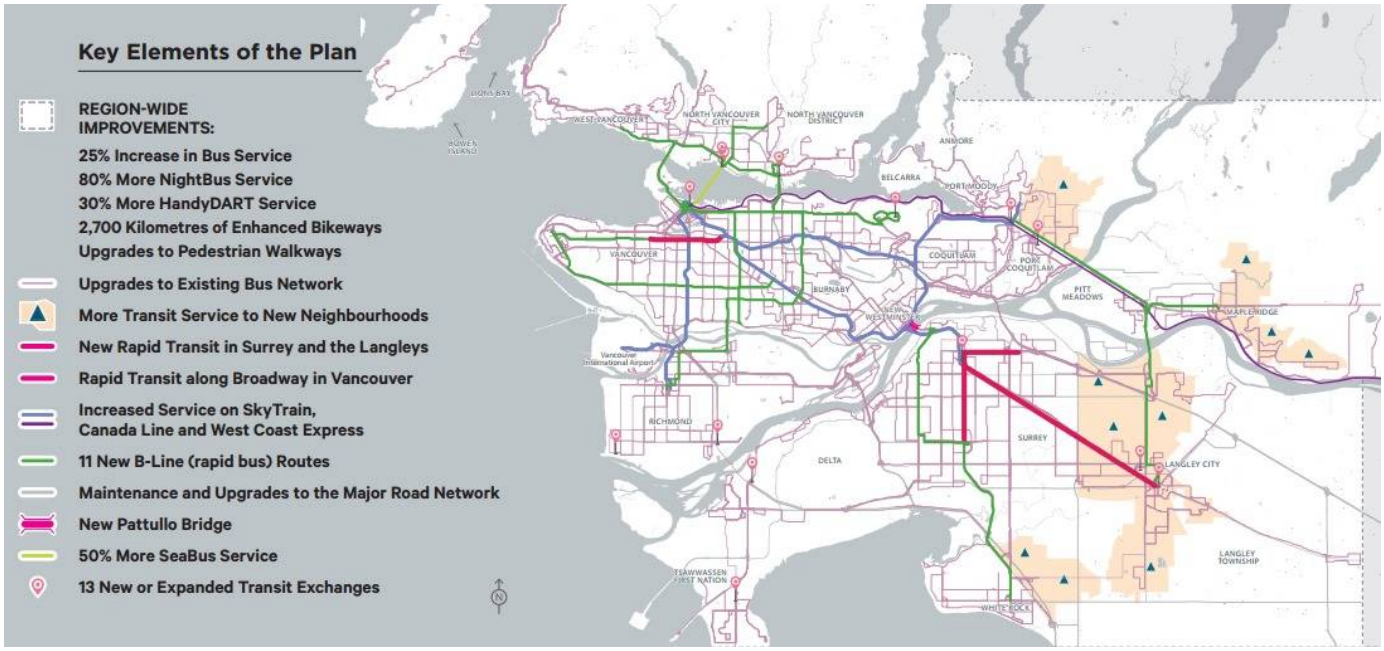
Re-attempt scheduled for future: Timing Unknown

Why the mechanism could be chosen in Vancouver

- To fund new transport initiatives across Metro Vancouver
- To gain large capital for major transport initiatives across the metropolitan region
- With taxes on vehicle fuel already popular as deterrent methods for vehicle users, and relatively accepted by the public, a sales tax was seen as a logical next step

Financial Specifications of Case Study

While Vancouver was less inclined to specify exact objectives and routes, the sales tax increase would support new bus routes, new express bus routes, increases in bus services, new rapid transit throughout the Metro Vancouver region, increased services on existing rapid transit, and improved transit interchanges, among other initiatives.



The proposed Vancouver tax increase would raise approximately $250 million per year. The cumulative total is projected at over $2.5 billion over ten years, using a 0.5% sales tax increase on existing rates. This would represent the region's contribution towards an overall $7.5 billion capital plan for transit and transportation investments, with the balance of funding coming from the provincial and federal governments. Government commitments would mandate that all funds gained from the sales tax would be entirely earmarked for new infrastructure and transit capacity.

The full $7.5 billion ten-year plan is a comprehensive approach to improve mobility for all residents in the region. It includes road improvements as well as transit infrastructure and expansion of services, but is focused on providing much-needed public transit schemes such as new light rail transit along central corridors and through rapidly-growing suburban regions.

Benefits

- Guaranteed large amounts of funding amount over a set period of time
- Government interventions can offset regressive tax effects for lower-income individuals
- Can set the amount to collect from the tax
- Public (government) control allows for public delivery of projects

Drawbacks

- Lacks specification of funding distribution
- Includes vehicle infrastructure upgrades, which could be prioritised
- Association with transport and political agendas can have positive or negative effect on public opinion
- Requires a referendum (generally) in order to pass

Assessment

Sales tax is a mechanism that, in the right circumstances, can generate a very large amount of revenue that is stable and easy to access. With strong political will, a sales tax increase provides a blanket source of funding. Despite the huge potential that this funding mechanism holds, difficulties with using this mechanism to fund public transport can arise in regions that are car dependent. The combination of a

poor public campaign and a strong car lobby led the first Vancouver transit referendum for a sales tax increase to fail; however, experts have attributed this to a political tension between the public and the transport authority within the region. Experts believe that a vast majority of the public understood the need and attractiveness of the proposed transit improvements, but were worried about how the sales tax increase would be responsibly handled by the transport authority, which is what swayed the vote.

Success of Financial Mechanism

With Sales Tax comprising a large portion of capital revenue, it follows that even a small increase can be used to generate large amounts of revenue from a guaranteed source of funding. However, the locations that Sales Tax is predominantly used in (chiefly North America) have a historical lack of public transportation initiatives compared to vehicle and road infrastructure. As such, the success of funding a project through Sales Tax depends on political will and public support (if there is a weaker political will).

As demonstrated by Vancouver, referendums regarding public transport are hit-and-miss, depending on public vote and political/authority campaigns. However, many successful examples within North America have shown that sales tax increases can be successful. Regions in Europe, it is felt, would potentially be more open to an increase in Sales Tax or VAT in order to fund public transport, given a generally more accepting public transport culture compared to North America.

Public Perception

Public perception of Sales Tax is difficult, as it affects every individual within the region that is undergoing the increase. As such, several public opinions will take part in the debate. However, two ways of overcoming the potential negative public perception can take place. First, government can get involved and run a lengthy strong campaign to properly inform the public on the issues surrounding public transport and the tax increase. Secondly, a public referendum (which is not always necessary depending on political will) can be bypassed in favour of a consultation and then decisive action on the part of the government and/or transport authorities.

Within Vancouver, public perception of the sales tax increase was warped to say no in opposition to the transport authority that would manage the extra sales tax influx, rather than vote for the issue of funding public transport. As such, public perception of the issue became a critical breaking point, through which the referendum that took place did not pass. If Vancouver and the provincial authorities had implemented the tax increase without a referendum, the difference in cost of goods would not have been as drastic compared to the quality of public transport that was implemented.

Future Prospects and Transnational Relevance

- Must acknowledge the difference between countries in regards to sales and goods' taxes, which impacts how the scheme is implemented: While Vancouver's 'tax-additional' model means that the final price is more daunting once additional tax is added, a model with tax included as VAT may be less of a noticeable impact to budgets and personal spending habits
- The failure of Vancouver is unique, as the politics behind the voter response overwhelmed the actual referendum question of whether public transport was necessary: This can be overcome through extensive public consultation campaigns and a stronger political will backing the push for increased public transport schemes
- Currently more effective in larger metropolises, with a greater tax payer foundation: Tends to have a greater economic and demographic range within the municipality, thus taxing a greater diversity of individuals rather than a particular demographic from a smaller region

As sales tax is more common in countries with stronger car-dependent behaviours, this makes it difficult to implement without a strong public support for public transport initiatives, or a strong government backing of the project. As well, difficulties in taxation methods across the world make each sales tax increase scenario unique to the location it is being implemented within. Despite this, variations of the

mechanism could be used to create a strong financing option for public transport in larger regions of Europe.

Furthermore, successful referendums in favour of sales taxes in regions such as Los Angeles demonstrate the viability of this mechanism in even the most car-focused of environments. Thus, despite the failings of Vancouver's referendum, it can be seen as a successful funding mechanism in many other locations, and depends predominantly upon public opinion and political leadership.

Transnational relevance: Europe-wide

Funding of major trasnport schemes is an issue faced by many cities and regions across the North West Europe Programme area and indeed more widely across Europe. Traditionally, in most countries tram-based links have been financed by public funding from national or regional government authorities, sourced from either taxation or borrowing or a combination. (In regimes where there is a national or regional transport infrastructure authority, operating profits may also assist).

But as with Sintropher partners, implementation of such schemes is facing a lack of available funding due to cuts in public expenditure following the European ecomic crisis of 2008 and subsequent efforts by national (or regional/city) governments, to recover. So innovative financing is of growing importance, and much can be learned from approaches in different European countries.

The financing approaches and city/region case examples on the reference resource are context-specific and reflect:

- the geographical context: the physical scale of the scheme and scale of capital cost. Obviously a major scheme with high capital cost of, say, €50m + may be beyond the resources of a single city or regional authority, and require a national contribution in a "cocktail" approach. The investment case will usually be stronger in a major dense metropolitan area than smaller regions with lower population and (possibly) lower or weaker economic activity.
- the organisational context: which level of government and/or relevant transport authority or agency is the primary initiator of the scheme - national, regional, or city - will influence the financing opportunities and options available.
- the legal context: the nature and extent of the powers and responsibilities of the initiating authority, and the processes/procedures, to actually pursue any of the financing approaches.
- But even though the various approaches and case examples are context-specific, their transnational relevance is strong:
- the approaches offer a stimulus and possibilities for wider thinking by cities and regions in other European countries, about how to assemble capital financing for transport schemes,
- in all countries, the reality of capital finance for transport infrastructure means that a "cocktail" approach is often the most practical way forward - and the approach of mixed public-private sector finance is an increasingly pragmatic basis
- some or all of the various approaches might be potentially adaptable within the particular organisational and governance regime of another country, using similar powers or processes
- the approaches offer possibilities for lobbying by city and regional authorities, in order to secure from national government the powers and competences to utilise new approaches (as has happened in the UK - for example local authorities have in recent years acquired powers to implement tax increment financing (TIF) although subject to safeguards over risk and borrowing; similarly, powers to enact a community infrastructure levy (CIL) on developments in their area, subject to local consultations and examination of viability and fairness for private developers.

The reference resource should be seen from this perspective, as a means to promote knowledge transfer and learning across different NWE countries and regions.

Further information

This paper was produced by UCL Bartlett School of Planning (Sintropher team members Charles King, Giacomo Vecia, Imogen Thompson) using desk research and expert comment. The paper reflects the views of the authors and should not be taken to be the formal view of UCL or Sintropher project.

The European reference resource can be accessed on the following:

Sintropher project website

http://www.sintropher.eu/publications

POLIS website

http://www.polisnetwork.eu/sintropher or http://www.polisnetwork.eu/res/resources

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