Local Government Priorities, Policies, and Programs Change as Money Becomes Scarce:

The City Fiscal Backdrop

Rethink. Recover. Rebuild: Reinventing Older Communities
Federal Reserve Bank of Philadelphia
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Philadelphia, Pennsylvania

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Changing Shape of Cities’ Fiscal Conditions

- Variations on a Revenue Theme
- Actions and Reactions
- Fiscal Mismatch and Contemporary Challenges
- Crystal Ball Gazing
Percentage of Cities "Better Able/Less Able" to Meet Financial Needs in Current Fiscal Year

Percentage of Cities "Better Able/Less Able" to Meet Financial Needs in Next Fiscal Year

Municipalities’ General Fund Revenue Composition, 2009

- Property taxes, 32%
- Sales taxes, 15%
- Income taxes, 4%
- Other taxes, 9%
- Fees & charges, 10%
- State funds, 12%
- Federal funds, 1%
- All other, 15%
Year-to-Year Change in General Fund Tax Receipts (Constant Dollars)

- 1995-96: 3.6% sales, 3.4% income, 2.0% property
- 1996-97: 4.2% sales, 1.5% income, 1.2% property
- 1997-98: 2.4% sales, 0.9% income, 1.4% property
- 1998-99: 2.8% sales, 1.0% income, 0.2% property
- 1999-2000: 6.0% sales, 0.1% income, 0.1% property
- 2000-01: 2.0% sales, 2.0% income, 0.2% property
- 2001-02: 4.4% sales, 0.6% income, 1.0% property
- 2002-03: 3.3% sales, 0.5% income, 2.2% property
- 2003-04: 4.0% sales, 2.3% income, 3.0% property
- 2004-05: 1.0% sales, 2.2% income, 2.3% property
- 2005-06: 1.0% sales, 2.2% income, 2.3% property
- 2006-07: 6.3% sales, 2.3% income, 2.3% property
- 2007-08: 6.2% sales, 2.3% income, 2.2% property
- 2008-09: 1.6% sales, 1.3% income, 1.6% property

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Increased Fees/Charges
New Fees/Charges
Increased Property Tax Rate
Development Fees

Revenue Actions FY09 (% of city finance officers listing factor)

- Increase fees – 45%
- Increase # of fees – 27%
- Increase property tax rate – 25%
- Increase level of impact fees – 19%
- Decrease property tax rate – 11%

City Spending Cuts in 2009

- Hiring freeze/layoffs: 67%
- Delay/cancel capital projects: 62%
- Cuts in other services: 33%
- Modify employee health benefits: 25%
- Across the board cut: 17%
- Cuts in public safety: 14%
- Renegotiate debt: 12%
- Cuts in human services: 11%

Figure 7: Revenue Actions in 2009

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Bureau of Labor Statistics

Industry: Manufacturing

Data Type: ALL EMPLOYEES, THOUSANDS
Bureau of Labor Statistics

Industry: Service-providing

Data Type: ALL EMPLOYEES, THOUSANDS

The graph shows the trend in the number of all employees in the service-providing industry from 1946 to 2006. The number of employees has steadily increased over the years, with a notable rise in the late 1980s and early 1990s, followed by a slight decline in the early 2000s before recovering in recent years.
Bureau of Labor Statistics

Industry: Leisure and hospitality

Data Type: ALL EMPLOYEES, THOUSANDS
Shift from Goods to Services

Source: Robert Tannenwald, *Are State and Local Revenue Systems Becoming Obsolete?*
Source: Donald Bruce and William Fox, “State and Local Sales Tax Revenue Losses from E-Commerce: Estimates as of July 2004” (University of Tennessee, Center for Business and Economic Research, July 2004)
http://cber.bus.utk.edu/ecomm/Ecom0704.pdf

Source: State and Local Government Sales Tax Revenue Losses from Electronic Commerce
By Donald Bruce, William F. Fox, LeAnn Luna. April 13, 2009
http://cber.utk.edu/ecomm/ecom0409.pdf
Exempt Property as Percentage of Total Assessed Value

- Multnomah Co., OR
- Hartford, CT
- Philadelphia
- Washington, DC
- New York

PILOT Revenue as Percentage of Budget

- Pittsburgh
- Philadelphia
- Minneapolis
- Indianapolis
- Detroit
- Boston
- Baltimore

States Move to Revoke Charities’ Tax Exemptions (February 27, 2010)

Provena-Covenant Medical Center v. (Illinois) Dept. of Revenue (2010)

Pittsburgh Pushes Tax on College Students
State Aid to Municipalities and to All Other Local Governments

- State aid as Percentage of General Municipal Revenue
  - 1971-1972: 24.1%
  - 1976-1977: 23.2%
  - 1981-1982: 20.8%
  - 1986-1987: 20.2%
  - 1996-1997: 20.7%
  - 2001-2002: 21.9%
  - 2006-2007: 19.6%

- State aid as Percentage of Total Local Government Revenue, Excluding Municipalities
  - 1971-1972: 36.8%
  - 1976-1977: 37.6%
  - 1981-1982: 38.2%
  - 1986-1987: 36.7%
  - 1991-1992: 37.3%
  - 1996-1997: 37.8%
  - 2001-2002: 38.1%
  - 2006-2007: 35.2%

- State Aid to Municipalities ($Millions)
  - 1971-1972: $40,358
  - 1976-1977: $45,450
  - 1981-1982: $40,613
  - 1986-1987: $46,470
  - 1996-1997: $61,064
  - 2001-2002: $71,887
  - 2006-2007: $68,838

- State Aid to Local Governments, Excluding Municipalities ($Millions)
  - 1971-1972: $127,806
  - 1981-1982: $163,194
  - 1986-1987: $194,268
  - 2001-2002: $337,677
  - 2006-2007: $335,011
# Federal Aid to Municipalities and to All Other Local Governments

## Tables

### Fed aid as Percentage of General Municipal Revenue

<table>
<thead>
<tr>
<th>Period</th>
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<tbody>
<tr>
<td>1971-1972</td>
<td>7.3%</td>
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<tr>
<td>1976-1977</td>
<td>14.7%</td>
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<tr>
<td>1981-1982</td>
<td>12.0%</td>
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<tr>
<td>1986-1987</td>
<td>6.4%</td>
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<tr>
<td>1991-1992</td>
<td>4.6%</td>
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<tr>
<td>1996-1997</td>
<td>5.3%</td>
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<tr>
<td>2001-02</td>
<td>5.3%</td>
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<tr>
<td>2006-07</td>
<td>5.3%</td>
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### Fed aid as Percentage of Total Local Government Revenue, Excluding Municipalities

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<tr>
<td>1971-1972</td>
<td>2.8%</td>
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<tr>
<td>1976-1977</td>
<td>6.2%</td>
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<td>1981-1982</td>
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<td>3.6%</td>
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<td>2006-07</td>
<td>3.5%</td>
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### Federal Aid to Municipalities ($Millions)

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<td>$12,145</td>
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<tr>
<td>1976-1977</td>
<td>$28,735</td>
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<tr>
<td>1981-1982</td>
<td>$23,500</td>
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<tr>
<td>1986-1987</td>
<td>$14,757</td>
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<tr>
<td>1991-1992</td>
<td>$12,119</td>
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<tr>
<td>1996-1997</td>
<td>$15,553</td>
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<tr>
<td>2001-02</td>
<td>$17,511</td>
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<td>2006-07</td>
<td>$18,487</td>
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### Federal Aid to Local Governments, Excluding Municipalities ($Millions)

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<tr>
<td>1971-1972</td>
<td>$9,633</td>
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<tr>
<td>1976-1977</td>
<td>$24,652</td>
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<tr>
<td>1981-1982</td>
<td>$21,927</td>
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<td>1986-1987</td>
<td>$19,357</td>
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<td>1991-1992</td>
<td>$17,953</td>
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<tr>
<td>1996-1997</td>
<td>$22,692</td>
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<tr>
<td>2001-02</td>
<td>$31,966</td>
</tr>
<tr>
<td>2006-07</td>
<td>$33,580</td>
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</tbody>
</table>

## Graph

- **Fed aid as Percentage of General Municipal Revenue**
- **Fed aid as Percentage of Total Local Government Revenue, Excluding Municipalities**
- **Federal Aid to Municipalities ($Millions)**
- **Federal Aid to Local Governments, Excluding Municipalities ($Millions)**

### Graph Notes

- Fed aid as a percentage of Total Local Government Revenue, Excluding Municipalities shows a similar pattern but with lower values, peaking in 1976-1977 at 6.2% and stabilizing at around 3.5% from 2001-02 to 2006-07.
- Federal Aid to Local Governments, Excluding Municipalities shows an increase from $9,633 in 1971-1972 to $33,580 in 2006-07.
Notes: a Income or sales tax for selected cities. b Cities can levy a local income tax, but no locality currently does so. c A local income tax under certain circumstances. d Sales tax only; cities can levy a property tax for debt-retirement purposes only. e Cities can impose the equivalent of a business income tax. f Sales taxes for selected cities and/or restricted use only.

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Crystal Ball Gazing

“It's tough to make predictions, especially about the future.” Yogi Berra
12-Month Change in Household Net Worth as a % of Nominal Gross Domestic Product
(Source: Federal Reserve, Bureau of Economic Analysis)
Personal Saving Rate (PSAVERT)
Source: U.S. Department of Commerce: Bureau of Economic Analysis

Shaded areas indicate US recessions.
2010 research.stlouisfed.org
How Bad Will It Get?

Total state budget shortfall in each fiscal year, in billions

Source: CBPP survey

Source: Elizabeth McNichol and Nicholas Johnson, “Recession Continues to Batter State Budgets: State Responses Could Slow Recovery” Center for Budget and Policy Priorities, February 2010
http://www.cbpp.org/files/9-8-08sfp.pdf
Fiscal Effects?

Tax receipts

Tax receipts

Tax receipts

Food tax

Lawn & Garden And Repairs

Underground?

Underground?

Reg Fee?

**Belt-Tightening in Bad Times**
Percent saying they have done ... because of the recession

- Bought less expensive brands or shopped more at discount stores: 57%
- Cut back spending on alcohol or cigarettes: 28%
- Reduced or cancelled cable or satellite TV subscription: 24%
- Changed to a less expensive cell phone plan or cancelled service: 22%
- Made plans to plant a vegetable garden: 21%
- Started doing yard work or home repairs that you used to pay for: 20%
- Held a garage sale or sold items on the Internet: 16%
- Had a friend or relative move in or you moved in with them: 10%
- Rented out a room or space in your home to a boarder: 2%

Question wording: I am going to read you a list of things that some people have done because of the economic recession but other people have not done. For each of the following, please tell me if you personally have done this, or not. Have you ...?
What to do?

- **The New Normal:**
  - Real estate market will be slow to recover: 2011-12?
  - Consumer spending and wages also down
  - Cities will tap into ending balances/reserves
  - Public concern will limit options

- **Don’t Waste a Crisis:** The economic shock of 2007 to the present ought to encourage a political discourse about reforming the architecture of municipalities’ revenue systems:

  1. **If States Want Cities to be Responsible for Their Actions, States Should Give Them Adequate Tools.** Diversify. Authorize access to taxes. Eliminate TELs.

  2. **The Fiscal Mismatch Is Weakening Cities.** Tax structures might be designed that link closer to cities’ underlying engines of growth or to income and wealth. Is a gross receipts tax (such as operates in Washington state, called the Business and Occupation Tax) a more accurate reflection of a city’s tax base?
3. **Reform Local Tax Systems.** Broaden the sales tax base. As the retail sales tax base has narrowed as a percent of consumer spending, is it time to reconsider a sales tax on services?

   Restructure the property tax. As real estate loses much of its value, as vacant properties lie fallow, and as the number and value of tax-exempt properties increase, cities should revisit their underlying fiscal architecture. E.g., Might cities consider moving from a uniform to a split-rate system? What’s lost and gained by exempting so much property from the tax roles?

4. **Jointly Provide Services and Share Service Delivery Costs.** Create regional taxing powers. Municipalities will be looking for regional partners and allies in designing a system that is less destructive to the region’s long-term interests and fairer in distributing the costs to the users.

5. **Pricing Drives Consumer Behavior and Often Disadvantages Cities.** Approximating the market value of city-delivered services would possibly reduce subsidies to free-riders. Commuter tax? Fee for service?
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