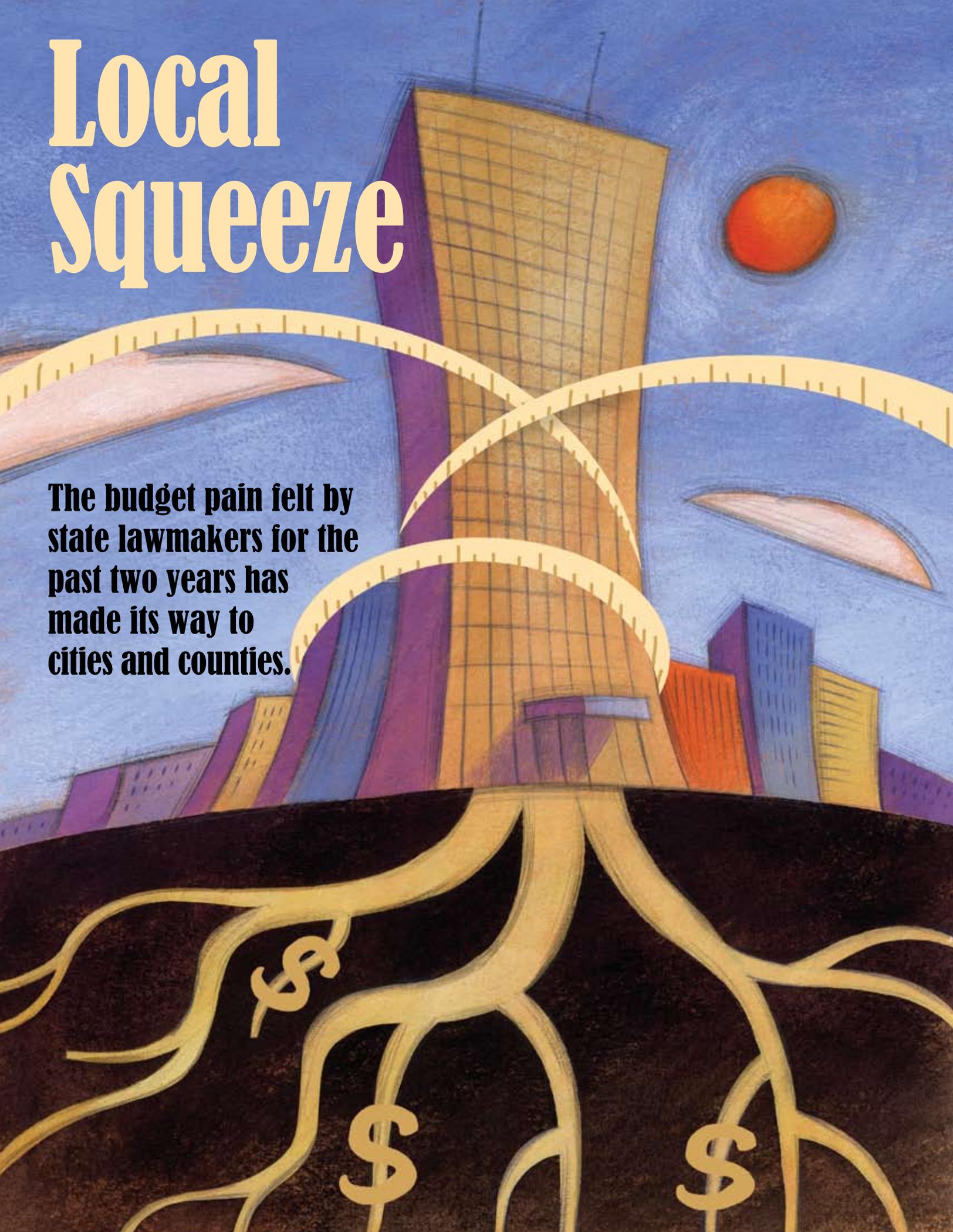


# Local Squeeze



**The budget pain felt by state lawmakers for the past two years has made its way to cities and counties.**

**BY ALAN GREENBLATT**

**C**ities and counties were largely spared the kind of shortfalls that decimated state budgets back in 2002 and 2003. During the current downturn, however, they are experiencing nearly as much pain as states.

In part, that's because of choices made by states. It's almost a given during tough times that legislatures will cut aid to local governments.

But while their woes are exacerbated by cutbacks from the state, local budget problems have their roots elsewhere. The reason localities were not hit as hard as states during the post-9/11 recession is that they depend largely on property taxes. Back then, those collections were still buoyant.

No more. The collapse of the housing market bubble and widespread foreclosures are eating into the local property tax base, with housing values down 10 percent since 2007. Commercial property values are continuing to decline, and localities face a long climb back. Tax collections lag market conditions because property appraisals, often done on a rolling basis, generally take two to three years to reflect diminished values.

The other major sources of local revenue—sales taxes and income taxes for those cities that collect them—are down as well. The result is that local governments expect to face at least two and possibly several more years of declining revenues.

City budget officers projected average budget shortfalls of 3 percent in 2009, with deeper holes in 2010 and 2011. The National League of Cities estimates that the municipal sector will face shortfalls of up to \$83 billion between 2010 and 2012.

"Austerities are not going to feel like one-year budget adjustments," says Mark Muro, policy director for the Brookings Institution's Metropolitan Policy Program.

**OFF LIMITS NO MORE**

It doesn't help that the fiscal pain felt by states has trickled down to the local and county levels. While few states still maintain

direct aid or general revenue sharing programs with their localities, most have complex fiscal relationships that, during downturns, come to involve changes in formulas that hurt localities.

"For anyone in local government, all you have to do is look to the state to see the threat," says David Smith, county manager in Maricopa County, Ariz.

His county sent \$66 million to the state of Arizona over the past two fiscal years and Smith expects the state to ask for an additional \$50 million this year.

This latest proposal is a shift that would move budget obligations away from the state and onto the books of counties. Counties would be expected to fund the entire Arizona

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ARKANSAS HOUSE MAJORITY LEADER**

Department of Juvenile Corrections, as well as 100 percent of the costs for incarcerating sexually violent prisoners. The budget proposal would cost Arizona's 15 counties a total of \$90 million, forcing them to raise property taxes and slash their own spending priorities.

Arizona is not alone. New Jersey proposes cutting local aid by 10 percent—or \$466 million—in FY 2011. When the Virginia General Assembly ended its session, lawmakers had adopted an \$82 billion budget and cut millions from education, health care and public safety.

Localities complain states have sticky fingers on everything from federal stimulus money to sales tax collections they're supposed to return to the municipalities that generated the purchases. The National League of Cities projects states, which transferred \$78 billion to cities in 2009, may shave that number by as much as \$30 billion over the next three years.

"Obviously, states are doing the traditional

**M**any cities are trying to find new sources of revenue, such as taxes on sodas and disposable grocery bags. Cities are trying to sell these taxes not only as money-raisers but virtuous in their own right, by helping to combat obesity and pollution, for instance.

Local governments increasingly have turned to such niche taxes and user fees in recent decades. For the most part, they are limited in the kind of broad-based tax increases they can impose. To some extent, that is because of the limits states put on their taxing authority.

And the structure of local taxes means they often have to wait for states to act. A city can't start collecting taxes on services that its state does not tax.

"If I'm a local government, I don't really have control over whether I have a sales tax or not, and what the base of that is," says Christopher W. Hoene, director of the National League of Cities' Center for Research and Innovation.

But the bigger limitation may be political. Voters have signaled that they do not want taxes going up during a period of economic uncertainty.

"In the long run, this new normal has to be faced first and foremost with reductions in services and spending," says Michael Coleman of the League of California Cities.

"Our experience has caused us to understand that you really have to convince your constituents that you are doing everything responsibly, within the limited means they've given you."

business of kicking the problem down the road—solving part of the state fiscal problem by reducing transfers to local governments," says John L. Mikesell, a government finance expert at Indiana University. "They've done that every recession, and they're doing it aggressively this time, as you might expect."

Legislators and other state officials describe the cuts in aid to localities as an unavoidable aspect of one of the worst budget seasons in memory.

"While it may be regrettable, cities have to take their share of the hit during a terrible budget year for states," says Representa-

*Alan Greenblatt is a news writer for npr.org and a former staff writer for Governing magazine.*

## NO BREAK ON COSTS FOR CITIES, COUNTIES



If revenues for local governments in the next several years are likely to grow at a snail's pace, costs are not.

The U.S. Government Accountability Office projects state and local expenditures on health care will continue to rise in coming years. No surprise there. A recent Boston Globe survey found that 25 communities in Massachusetts now devote, on average, 14 percent of their budgets to health care—up from 8 percent a decade ago.

Municipal health plans in Massachusetts, as in other states, offer benefit levels that are higher and copayments that are lower than most private-sector plans and often include generous coverage for retirees.

Because personnel costs tend to dominate city and county budgets, local officials are pressing public employee unions to make concessions that might have seemed inconceivable just a few years ago. Employees are being asked to contribute more to their own health plans. New hires, in particular, are being promised less generous retirement benefit packages than employees with longer tenure.

Municipal employee unions are negotiating in hopes of avoiding layoffs and deeper pain.

"Taxpayers, who are paying our salaries, are happy to have any salary," says Jay Williams, the mayor of Youngstown, Ohio. "When they see public employees unwilling to make small sacrifices, public opinion is very different than it was three years ago."

Throughout California, as in other states, local governments are calling on their employees to make sacrifices. Last year, San Diego Mayor Jerry Sanders negotiated a package of salary and pension cuts with most of the city's unions that saved San Diego \$43 million—money that would otherwise have had to come from layoffs and closing libraries and recreation centers, he said. In San Jose, which has suffered shortfalls in each of the last nine years, all but two employee unions last year agreed to "true zeros." That means no raises and no step increases within their pay grades.

This year, San Jose is facing a much larger shortfall of \$116 million. In part, that's because the state is withholding \$45 million the city once counted on. It also has a lot to do with the \$1 billion dollar loss the city's retirement funds have taken recently in the financial markets.

San Jose now spends \$29 in retirement costs for every \$100 in salary for most employees, with an even greater outlay for those working in public safety. During the past nine years of budget cutting, the city's average cost per employee has gone up 64 percent, while revenues have gone up only 18 percent, says Michelle McGurk, senior policy adviser to Mayor Chuck Reed.

Reed is now asking every bargaining unit in the city to give back 10 percent to 15 percent of their compensation package to avoid layoffs. "We think that will go down to the wire in June," McGurk says.

That certainly seems likely. But further cuts appear inevitable.

*"Cities are having a debate about defining what their core services are and what the city wants to be."*

CHRISTOPHER W. HOENE,  
NATIONAL LEAGUE OF CITIES

tive Steve Harrelson, majority leader of the Arkansas House.

### THE STATE OF CITIES

The diminished financial circumstances of cities and counties are forcing them to confront some difficult choices. They are cutting areas that have traditionally been sacrosanct, such as public safety. And they are attempting in many places to trim salaries and benefits offered to unionized workers.

That's a fight that most localities, at least until recently, had been unwilling to take on. Today, they feel they have no choice.

"The scope of the downturn is such that parts of the budget that used to be off limits aren't anymore," says Christopher W. Hoene, director of the National League of Cities' Center for Research and Innovation. "Cities are having a debate about defining what their core services are and what the city wants to be."

Major cities across the country have taken difficult steps, particularly with regard to personnel, to combat budget shortfalls that in the largest cities are topping the billion-dollar mark. San Francisco Mayor Gavin Newsom in March sent pink slips to 17,000 of the city's 26,000 workers, laying them off with the intention of offering them a shorter work week. Newsom backed down when the unions balked, instead imposing 12 unpaid



**HOUSE MAJORITY  
LEADER  
STEVE HARRELSON  
ARKANSAS**

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furlough days. The move was expected to save the city, which faces a \$522 million shortfall in the coming fiscal year, about \$100 million.

Chicago, which faced a \$520 million shortfall for FYI 2010, used more than \$200 million from a reserve fund created by its long-term lease of parking meters. City workers also accepted 24 unpaid furlough days and the elimination of paid city holidays and overtime pay. In Dallas, which has a budget gap of \$100 million, most departments are looking at a 30 percent cut, while police and firefighters face a 5 percent cut.

Almost every large city is shedding jobs, but smaller localities are making deep cuts as well. When Bossier City, La., faced a shortfall of \$6.5 million in its \$50.3 million budget last year, Mayor Lorenz “Lo” Walker proposed eliminating 117 of 897 city positions, including 80 in the police and fire departments. Dover, Del., closed its shortfall of \$10.5 million in part by requiring all city employees to take 12 furlough days. Springfield, Ill., projects a shortfall of up to \$12 million in its coming fiscal year and anticipates eliminating up to 192 positions.

Cities and counties will have to keep cutting for the next couple of years, with very few jurisdictions talking seriously about broad-based tax increases. Instead, they are starting to examine fundamental questions about their priorities.

Localities are eliminating amenities such as summer camp facilities and school planetariums. But they are also trying to avoid wholesale elimination of such services as senior centers, parks and libraries.

“A city can’t be just about police, fire and paving roads,” says Hoene of the National League of Cities.

#### **PROBLEMS HERE TO STAY**

As localities grapple with the question of what services they’ll continue to provide, they have to reckon with the reality that their revenue problems are here to stay. This is not just a bad spell brought on by recession.

“In California, we have some long-term structural problems that predate the economic downturn,” says Michael Coleman, fiscal policy adviser to the League of California Cities. The most obvious one is tax limitations.

Like states, cities and towns base most of their sales taxes on goods, not services. The political difficulty of taxing services keeps local governments from capturing most of the growth in the economy. The federal Government Accountability Office projects that state and local sales tax collections as a share of gross domestic product will continue to decline over the next five years.

State and local budget officers predict that revenues will grow at a much slower rate over the next several years than they have in recent decades. Although there’s been a lot of talk about states and cities facing a “new normal” of sluggish growth, Hoene says what’s happening at the local level is really “a return to the old normal.”

He believes the robust financial picture of most of the past decade was an aberration, masking underlying problems. “What the economists are telling us is that the growth in the economy and growth in revenues will not be at the same level we saw in late ’90s and early 2000s,” Coleman says. “It will be much more modest.”

 **CHECK OUT** more on state budget gaps and steps states are taking to balance budgets at [www.ncsl.org/magazine](http://www.ncsl.org/magazine).