

# The Quest for Cost-Efficient Local Government in New England: What Role for Regional Consolidation?

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The views expressed in this presentation are those of the speaker and do not necessarily represent positions of the Federal Reserve Bank of Boston or the Federal Reserve System.

## Local governments face ongoing budgetary strains.

- The housing crisis and Great Recession have hit local governments hard.
  - Falling property values have eroded the property tax base.
  - States have reduced local aid.
- More austerity lies ahead.
  - Federal government likely to cut grants to states and localities.
  - Health care and pension obligations will squeeze into discretionary spending.
- Localities are likely to need structural spending reforms, not just temporary measures.

# Local government structure contributes to localities' budgetary strains.

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- “Our local service delivery method is not financially sustainable.” [interview with Massachusetts government official]
- “We are frugal within towns, but our overall system is not frugal.” [interview with Maine economic development expert]
- “Coordination across political boundaries creates economies of scale and improves the fiscal health of cities.” [National expert on city finances]
- “Efficiencies, consolidations, and realignments [of local governments and education systems] will free up scarce resources to meet our state’s pressing priorities.” [Connecticut Institute for the 21<sup>st</sup> Century]

# To what degree could regional consolidation alleviate budgetary strains?

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- Some moves toward greater regionalization are making headway, but they are not yet broadly visible.
- Questions my research addresses:
  - What is the potential scope of regionalization?
  - How large are the savings likely to be?
  - What are the implications for service quality?
  - What actions by state governments would help get us from where we are now to where we should be?
- My research does not recommend an optimal level of regionalization, as this depends on specific local concerns in addition to cost savings.

## What is “regionalization” or “regional consolidation”?

- Study does not address cross-state collaboration.
- Study does not address mergers of local governments.
- Focus is on mechanisms that maintain localities as distinct units but consolidate service provision across jurisdictions.
  - Intermunicipal (or “interlocal”) partnerships allow multiple localities to provide specified public services jointly.
  - Centralization of services (“shared services”) entails transfer of responsibility for municipal services to a state or regional authority.

## Key conclusions

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- A strong case exists for regionalizing selected services, based on both cost and quality considerations.
- Regional consolidation does not offer immediate, major relief from budgetary strains, but should be part of a longer-term strategy.
- States could encourage further regional consolidation by adopting stronger and more targeted regulations and fiscal incentives.

# Outline of today's presentation

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- Overview of nationwide findings on economies of scale and regional consolidation of local public services.
- Case studies of three local public services, providing for each:
  - Data on fragmentation of service delivery for all six New England states
  - Cost saving analysis for Massachusetts and Connecticut
  - Policy options for creating incentives for consolidation
- Summary of findings and common themes.

# Economies of scale for local public services: main insights from experiences and research

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- Not all local public services can be provided more cost-effectively on a larger scale.
- Capital-, technology-, and expertise-intensive services often exhibit economies of scale.
- Other considerations in considering regional consolidation:
  - Service quality
  - Bargaining or purchasing clout
  - Risk-sharing
  - Externalities
  - Equity



# Evidence differs across services, but some findings are clear and well-documented.

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- “Governments have been centralizing emergency dispatch services with considerable success.”
- “Public health is ... inherently more of a state or federal service than it is a municipal service” ... “The existing use of centralized, regionalized, or contracted services is testimony to the fact that many municipalities have looked for a larger and more cost-effective solution.”
- “Expert tasks in finance, administration, purchasing, and IT systems development are strong candidates for regional provision.”

Source: Holzer and Fry, *Shared Services and Municipal Consolidation: A Critical Analysis* (2011). Also covered in report of Massachusetts Regionalization Advisory Commission (2010).

# What share of city and town budgets goes to services that should be regionalized?

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- Roughly 20 percent of local government spending goes to services that are characterized by demonstrated economies of scale (national estimate by Holzer and Fry 2011).
  - \$4.8 billion in Massachusetts
  - \$2.7 billion in Connecticut
  - \$700 million in Rhode Island
- Remainder of talk focuses on how much savings could be achieved in three areas:
  - Local public safety: Emergency call handling and dispatch
  - Local public health services
  - Local public employee retirement systems (as example of high-level finance and administration services)
- Massachusetts and Connecticut likely could achieve high percent savings by consolidating these services.

# Example #1: Emergency call handling and dispatch is very fragmented in southern New England.

Fragmentation of New England's Public Safety Answering Point (PSAP) System					
		Per 100K Population		Per 1,000 Square Miles	
	Total PSAPs	Number	Rank (1=Most Fragmented)	Number	Rank (1=Most Fragmented)
<b>Connecticut</b>	<b>111</b>	<b>3.1</b>	<b>19</b>	<b>22.9</b>	<b>4</b>
Maine	26	2.0	32	0.8	39
<b>Massachusetts</b>	<b>268</b>	<b>4.1</b>	<b>12</b>	<b>34.2</b>	<b>2</b>
New Hampshire	4	0.3	50	0.4	46
Rhode Island*	72	6.8	3	68.9	1
Vermont	8	1.3	41	0.9	38
New England	489	3.4		7.8	
United States	6,863	2.2		1.9	

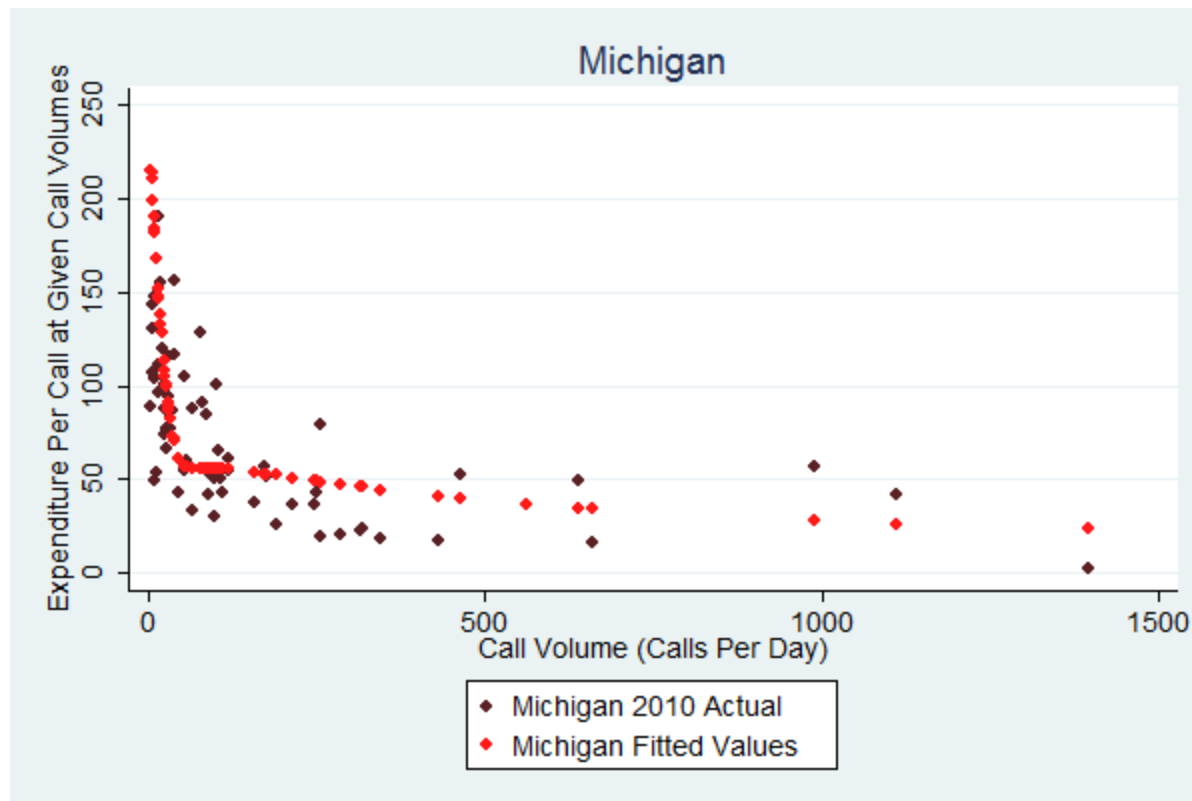
Source: Author's calculations based on FCC Master Registry as of December 2011 and 2010 Decennial Census

\*State of Rhode Island reports having far fewer PSAPs than indicated in FCC Master Registry

# Methodology for estimating cost savings from consolidating PSAPs

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- Step 1: Use administrative data from Michigan, Maryland, and Pennsylvania to estimate PSAP cost curves.



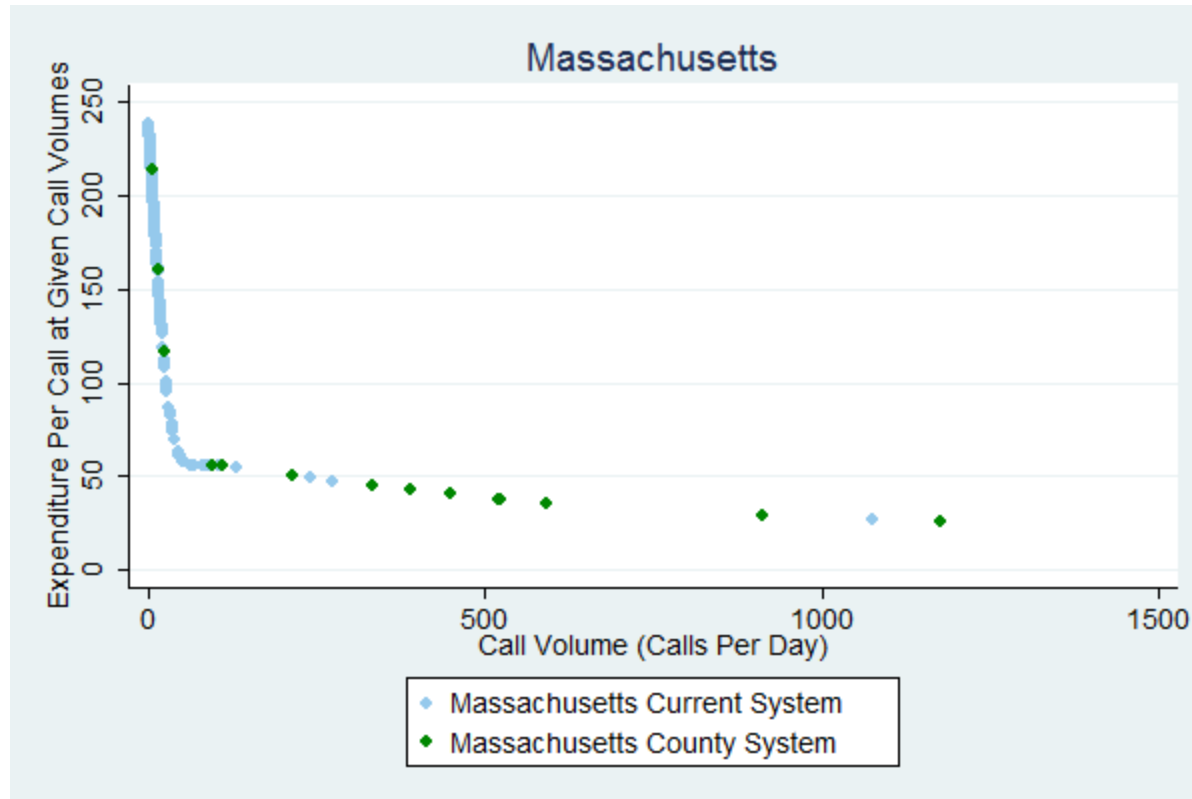
# Methodology for estimating cost savings from consolidating PSAPs (continued)

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- Step 2: Use these relationships between cost per call and call volume to estimate the costs of operating the current PSAPs in Massachusetts and Connecticut.
- Step 3: Then use these same relationships to estimate the hypothetical costs of operating consolidated PSAPs in Massachusetts and Connecticut.  
For illustration, show county-level configuration.
- Step 4: Compare estimated total costs under the current and consolidated structures.

# Consolidating Massachusetts PSAPs by county would reduce expenditure per call.

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# Consolidating to 14 regional call centers in Massachusetts would reduce operating costs by more than one-half.

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## Estimated Massachusetts Public Safety Answering Point (PSAP) Costs

Based on data from:	Michigan	Maryland	Pennsylvania
Current Structure (Millions)	\$182.8	\$132.8	\$192.1
County Structure (Millions)	\$71.4	\$46.1	\$73.7
Total Savings (Percent)	60.9	65.3	61.6

Source: Author's calculations based on data from Michigan State 9-1-1 Committee 2011 Annual Report to the State Legislature, Maryland Emergency Numbers Systems Board 2010 Annual Report, Pennsylvania Emergency Management Agency Bureau of 9-1-1 2010 Annual Report, and the Massachusetts State 9-1-1 Department

# Consolidating to 8 regional call centers in Connecticut would also significantly reduce operating costs.

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## Estimated Connecticut Public Safety Answering Point (PSAP) Costs

Based on data from:	Michigan	Maryland	Pennsylvania
Current Structure (Millions)	\$117.0	\$101.0	\$117.6
County Structure (Millions)	\$50.3	\$37.4	\$52.5
Total Savings (Percent)	57.0	63.0	55.4

Source: Author's calculations based on data from Michigan State 9-1-1 Committee 2011 Annual Report to the State Legislature, Maryland Emergency Numbers Systems Board 2010 Annual Report, Pennsylvania Emergency Management Agency Bureau of 9-1-1 2010 Annual Report, and the Connecticut Office of Statewide Emergency Telecommunications E-911 Total Call Volume Reports



# Other states have already undertaken large-scale PSAP consolidation.

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<b>Public Safety Answering Point (PSAP) Consolidation Since 2001</b>				
<b>States with a High Share of PSAPs Closed</b>				
<b>State</b>	<b>Number of Closed PSAPs</b>	<b>Number of Current PSAPs</b>	<b>Percent Closed</b>	<b>National Rank Based on Percent Closed</b>
Maine	41	26	61.2	1
North Carolina	165	140	54.1	2
South Dakota	52	45	53.6	3
Washington	28	71	28.3	4
Vermont	3	8	27.3	5
Michigan	67	179	27.2	6
Hawaii	2	6	25.0	7
Nebraska	25	83	23.1	8
Missouri	50	176	22.1	9
Tennessee	38	165	18.7	10

Source: FCC PSAP Master Registry as of December 13, 2011

# Getting from here to there: state-level incentives and funding for PSAP consolidation

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- Legislative mandate specifying target number of PSAPs (Maine).
- State-imposed technological or staffing requirements for PSAPs (North Carolina, South Dakota)
- Reduced state operational funding for non-consolidated PSAPs (North Carolina, Washington, New Mexico; Connecticut uses 40,000 population threshold).
- State funding for investments in consolidated facilities (North Carolina; Essex County, Massachusetts).

## Example #2: Massachusetts and Connecticut have among the most fragmented local health systems in the nation.

Fragmentation of New England's Local Health Department (LHD) System					
		Per 100K Population		Per 1,000 Square Miles	
	Total LHDs	Number	Rank (1=Most Fragmented)	Number	Rank (1=Most Fragmented)
<b>Connecticut</b>	<b>77</b>	<b>2.2</b>	<b>9</b>	<b>15.9</b>	<b>2</b>
Maine	10	0.8	27	0.3	35
<b>Massachusetts</b>	<b>330</b>	<b>5.0</b>	<b>2</b>	<b>42.1</b>	<b>1</b>
New Hampshire	5	0.4	35	0.6	27
Rhode Island	1	0.1	49	1.0	23
Vermont	12	1.9	10	1.3	17
New England	435	3.0		6.9	
United States	2,566	0.8		0.7	

Source: Author's calculations based on data from National Association of County and City Health Officials (NACCHO) 2010 survey of public health departments.

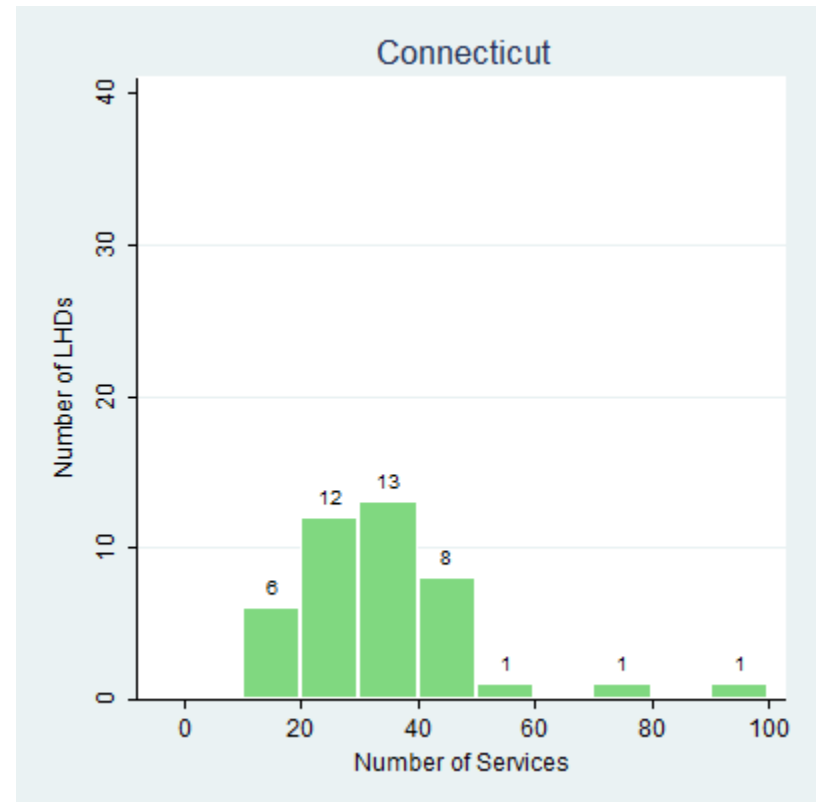
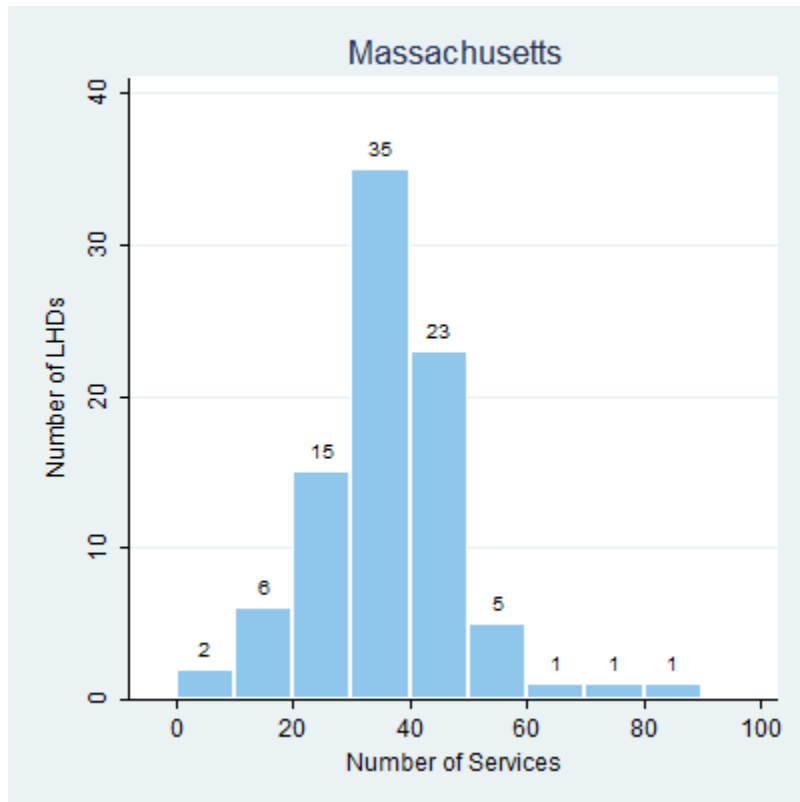
Massachusetts and Connecticut spend relatively little on local public health because many of their health departments provide limited services.

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<b>Median Annual Per Capita LHD Expenditures</b>	
<b>Expenditure Per Capita</b>	<b>Number of States</b>
<b>&lt;\$20.00</b>	<b>6 ( including Massachusetts and Connecticut)</b>
<b>\$20.00-\$54.99</b>	<b>24</b>
<b>\$55.00 or more</b>	<b>10</b>

Source: National Association of County and City Health Officials (NACCHO) 2010 survey of public health departments  
Note: The following states had no data or insufficient data and were not included in these totals: Hawaii, Maine, Mississippi, Nevada, New Hampshire, New Mexico, Rhode Island, South Dakota, Tennessee, and Vermont

# The extent of service provision varies widely across Massachusetts and Connecticut localities.



Source: Author's calculations based on data from National Association of County and City Health Officials (NACCHO) 2010 survey of public health departments

# Methodology for estimating cost savings from consolidating Local Health Departments

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- Step 1: Using national data, estimate the relationship between Local Health Department size and cost per capita (controlling for differences in service levels)
- Step 2: Calculate a “rounded” service level for each county in Massachusetts and Connecticut
- Step 3: Estimate total health department expenditures under a county-level, “rounded” service model in Massachusetts and Connecticut
- Step 4: Compare estimated total costs under the current and consolidated structures

# Consolidation could reduce local public health costs by 25 percent in Massachusetts and 13 percent in Connecticut.

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<b>Estimated Local Health Department (LHD) Costs</b>		
	<b>Massachusetts</b>	<b>Connecticut</b>
<b>Current Structure (Millions)</b>	<b>\$59.9</b>	<b>\$61.4</b>
<b>County Structure with “Rounded Services” (Millions)</b>	<b>\$30.4</b>	<b>\$36.0</b>
<b>Total Savings (Percent)</b>	<b>49.2</b>	<b>41.3</b>
<b>From Service Reductions in High-Service Cities and Towns (Percent)</b>	<b>24.3</b>	<b>28.1</b>
<b>From Economies of Scale (Percent)</b>	<b>24.8</b>	<b>13.2</b>

Source: Author's calculations based on data from National Association of County and City Health Officials (NACCHO) 2010 survey of public health departments

# Alternative approaches to achieving consolidation of local health departments

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- State controls local health services (Florida, Rhode Island).
- State provides partial funding on a sliding scale, depending on extent of regionalization (Utah, Connecticut).
- Define accreditation standards and tie state funding to accreditation (Connecticut moving in this direction).
- Massachusetts recently began to finance Local Health Districts that promote coordination and resource sharing among local health departments.



# Example #3: Massachusetts, Connecticut, and Rhode Island public pension systems are among the most fragmented in the nation.

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Fragmentation of New England's Public Pension Systems					
		Per 100K Population		Per 1,000 Square Miles	
	Total Plans	Number	Rank (1=Most Fragmented)	Number	Rank (1=Most Fragmented)
<b>Connecticut</b>	59	1.7	6	12.2	4
Maine	1	0.1	44	0.0	47
<b>Massachusetts</b>	100	1.5	7	12.8	2
New Hampshire	4	0.3	27	0.4	21
<b>Rhode Island</b>	13	1.2	9	12.4	3
Vermont	5	0.8	17	0.5	18
New England	182	1.3		2.9	
United States	2,540	0.8		0.7	

Source: Author's calculations based on 2007 Census of Governments and 2010 Decennial Census

# Methodology for estimating savings from public pension consolidation

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- Step 1: Using national data, estimate the relationship between pension size and administrative cost per member
- Step 2: Generate two hypothetical consolidated plans: all local plans consolidated, and all local and state plans consolidated
- Step 3: Estimate total administrative costs under these two consolidated structures
- Step 4: Compare estimated total costs under the current and consolidated structures

Moving to a state-local consolidated pension plan would reduce local administrative costs by about 40 percent in both Massachusetts and Connecticut.

<b>Estimated Local Public Pension Administration Costs</b>					
	<b>Current Structure</b>	<b>All Local Plans Consolidated</b>		<b>All Local Plans Consolidated with State Plans</b>	
	<b>Costs (Millions)</b>	<b>Costs (Millions)</b>	<b>Savings (Percent)</b>	<b>Costs (Millions)</b>	<b>Savings (Percent)</b>
<b>Massachusetts</b>	<b>\$86.4</b>	<b>\$53.7</b>	<b>37.8</b>	<b>\$48.7</b>	<b>43.7</b>
<b>Connecticut</b>	<b>\$19.4</b>	<b>\$16.6</b>	<b>14.5</b>	<b>\$11.0</b>	<b>43.1</b>

Source: Author's calculations based on Census Bureau data on Retirement Systems, 2002–2008

# Pension plan consolidation in practice

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- Motivation is usually to enhance labor mobility (not to save costs).
- Phase-in is gradual as statewide plans absorb smaller plans.
  - Wisconsin achieved full consolidation of state & local plans over three decades (1947-1977).
  - Colorado, Florida, New York, and Maine have consolidated plans with outstanding exceptions.
- Most likely consolidation scenarios for other states:
  - Enroll new state and local employees in statewide plan.
  - Merge plans for employees/retirees of distressed cities and towns into statewide plan (possible scenario for Rhode Island?).
- Massachusetts and Connecticut have implemented some consolidation of asset management (local plans can have state manage their investments).

# Summary and conclusions

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- Southern New England states are good targets for regional consolidation because they have fragmented local public service provision.
- Consolidation efforts should target local services whose costs can be reduced substantially without sacrificing quality.
- Achieving substantial savings would require consolidating multiple services across multiple cities and towns.
- For some services, consolidation could be used to raise quality without increasing costs.
- States should consider incentives and stronger regulations to promote substantial consolidation of local public services.

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