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The Fiscal Health of Wisconsin Cities and Villages and Policy Reponses

Craig Maher
Department of Political Science
University of Wisconsin-Oshkosh

Steven Deller
Department of Agricultural and Applied Economics
University of Wisconsin-Madison/Extension

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Summary

A web-based survey of fiscal health was administered to all Wisconsin cities and villages during the early summer of 2004. A total of 155 municipalities responded to the survey. Of those responding, 53.5 percent reported that their current revenue base is inadequate and more than 58 percent responded that their fiscal condition in five years will be inadequate. Some of the strategies most actively pursued in response to fiscal stress include the adoption or increase in user fees and charges, refinance outstanding debt and delaying capital expenditures. Strategies least likely to be pursued include increasing short-term debt and workforce reductions.

Introduction

A great deal has been said in recent years about the plight of local government finance in Wisconsin. Local officials tend to emphasize limited state aid growth and state officials have tended to focus on the rate of property tax growth. This study takes an objective look at the fiscal condition of Wisconsin municipalities through the lenses of municipal officials. More specifically, through the use of a web-based survey we sought to learn the degree of fiscal stress facing municipalities and the strategies being implemented to cope with fiscal stress.

The fiscal health and well-being of local governments is important.[1] Above all, it is an indication of the ability of local governments to provide adequate and uninterrupted services to local residents and businesses. While fiscal health may not be the ultimate measure of success for local governments, a fiscally unhealthy local government will not be able to provide the level and quality of public services that are required for a high quality of life, sound local economy and an effectively functioning government.

When the library reduces hours of service, the roads are full of potholes, emergency services are slow to respond, or water treatment facilities are at capacity and there are no funds for expansion, local residents and businesses will perceive a problem. Trying to identify and deal with fiscal problems before they get out of hand is vastly better then trying to cope with a full-blown crisis. In this light attending to local fiscal health is akin to taking an ounce of preventive medicine to avoid taking a pound of cure.

Understanding the fiscal health of individual local governments is important to local officials, taxpayers, businesses, potential investors and other concerned parties with a stake in the services and finances of the community. Local officials must be able to understand and effectively communicate their jurisdiction's fiscal condition to people who do not necessarily have a public finance background. Whether they are trying to explain a proposal to raise taxes, cut services, charge fees for services, or issue new debt, it is helpful for local officials to be able to articulate the financial rationale for their actions.

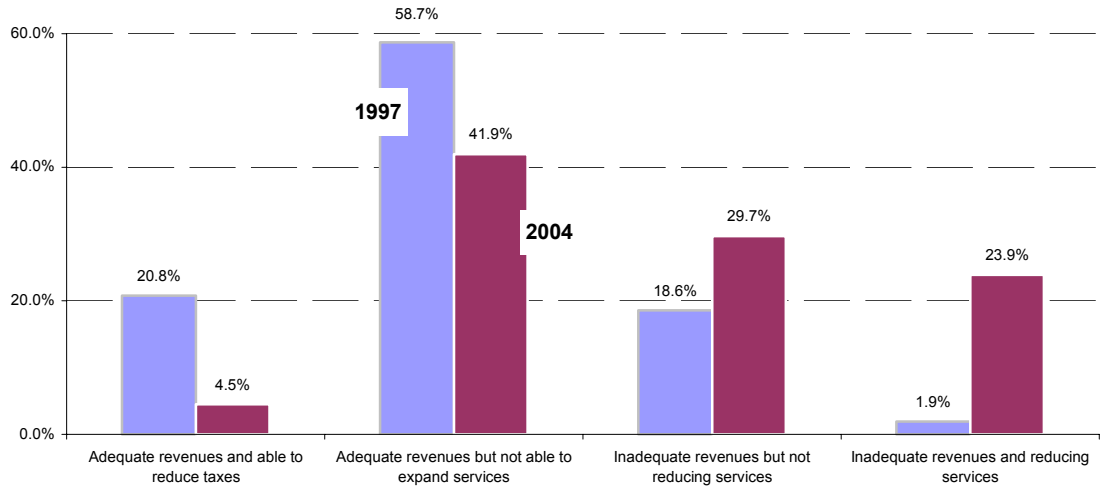
Local government fiscal health is important not only because it has to do with the jurisdictions to finance needed services. There are additional reasons why local leaders should want to improve their jurisdictions fiscal health, not the least of which is to get reelected by the voters. Other reasons for maintaining fiscal health include the fiscal health influences on homeowner location decision, business location decisions and economic development, local government organizational flexibility and human resources quality, local government

[1] This introductory material draws on Honadle, Costa and Cigler (2004).

competitiveness, service provision quality and variation in services provided, long-term credit worthiness and tax costs to local residents and businesses.

Unfortunately, the combined impacts of the recent economic recession, declining support from the state and significant uncertainty over future spending restrictions embodied in the Taxpayers Bill of Rights (TABOR) have created a situation of significant fiscal stress for Wisconsin cities and villages.[2] In a survey of cities in villages conducted in 1997, less than one in five municipality expressed concern about the adequacy of their fiscal position (Deller, Hinds and Hinman 2001). Today the fiscal health of Wisconsin municipalities has fundamentally changed for the worse (Figure 1 and Table 1). In general, 53.5 percent of the respondents believe that their revenues are "inadequate" and 23.9 percent are facing reductions in services in response to their current fiscal position. Only 4.5 percent of the respondents reported that their revenues are adequate and they are able to reduce local taxes. This stands in stark contrast to 20.8 percent of respondents to the 1997 survey who claimed that their fiscal health was sufficiently strong that they were able to reduce taxes. Almost one in five municipalities (23.9%) report that their fiscal health is sufficiently stressed that they are faced with the reduction of services.

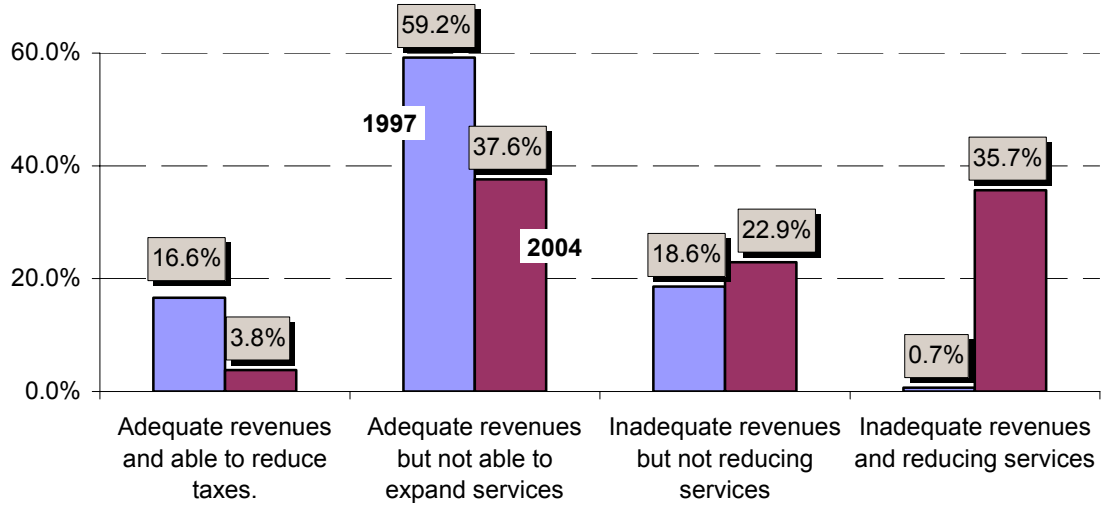
Figure 1. Current and Historical Financial Condition



If we ask municipal officials to consider their future (five years) fiscal health, the picture becomes bleaker (Figure 2 and Table 1). A clear majority (58.6%) believe that their revenues will be inadequate and 35.7 percent report that they will be forced to reduce services. Only 3.8 percent believe that they will be in a position to reduce taxes. Compare these results to the same question asked only seven years earlier: a clear majority of respondents in 1997 believed that they had adequate revenues over the next five years and 17 percent thought that they would be able to reduce taxes! The combined affects of the recent economic recession and uncertainty over state funding policies has created a direr fiscal outlook for most Wisconsin municipalities. A significant part of this pessimistic outlook in 2004 is due to the uncertainty surrounding state shared revenues and the serious attention being paid to the proposed Taxpayers Bill of Rights (TABOR). Until the state resolves some of its long-term fiscal issues, municipalities in Wisconsin will face significant uncertainty.

[2] According to Osborne and Hutchinson (2004), a similar pattern can be found in most other states.

Figure 2. Expected Future Financial Condition



Research Goals

The intent of this applied study is to document the current fiscal health of Wisconsin cities and villages as described by city and village officials and examine the strategies that municipalities are adopting to cope with the current situation. To gather the necessary information a web-based survey was conducted during early summer of 2004. Local officials were notified by e-mail notices and post cards. A total of 155 city and village officials responded. Beyond these brief introductory remarks the study is composed of three parts. In the next section we descried discuss the results on current fiscal conditions. We then describe what strategies local officials are pursuing to adapt to their fiscal situation. We close the discussion with a brief overview of some broad-based strategies that municipalities can pursue to improve their long-term fiscal health.

Current Fiscal Conditions

The survey asked eight questions to more specifically gauge the fiscal health of Wisconsin municipalities. The results suggest several areas of concern (Table 2), for instance:

- less than half (45 percent) agree that their fiscal situation is acceptable;
- only 37 percent of the municipalities have a fully financed capital improvements plan;
- 41 percent of the communities are near their debt limit;
- less than half (48 percent) are satisfied with their current credit rating; and
- 45 percent are faced with unfunded pension responsibilities

Perhaps of greater concern is that 40.8 percent are at or near their debt limit. Because most capital improvement projects are funded through debt, an alarming number of Wisconsin cities and villages may not be in the position to finance major capital projects. Another concern facing Wisconsin municipalities is future pension obligations for municipal employees. Almost half (45.1%) reported that they unsatisfied with their position on pension funding. As we age as a society the number of public employees retiring will increase significantly placing many municipalities under additional stress.

The few "bright" spots in this series of survey questions include:

- 52 percent are able to maintain three months of operating reserves with current cash reserves; conversely 40 percent are unable to do so; and
- 54 percent have been able to roll over cash reserves from the previous budgeting cycle, whereas only 32 percent have been unable to do so

Based on these survey results, many Wisconsin cities and villages may not be in crisis mode, but current trends are unsustainable. As the state grows and demand for municipal services expands, many will be in a difficult position to satisfy those demands. The combination of concerns over debt limits, credit rating, unfunded pension obligations and instability of state aids paints a picture of potential crisis on the near-term horizon.

Current Strategies Being Adopted

There are numerous short- and long-term strategies that municipalities can pursue when faced with fiscal stress. For this study we focused on three broad categories: service delivery or management, revenue alternatives and changes in expenditure policies. We asked respondents to indicate the degree to which they agree or disagree with the listed strategies as they describe their community's recent efforts to cope with fiscal stress. We do not attempt to address the political viability of the alternative strategies, but rather seek to gain insights into the current thinking of local officials. We will discuss each in turn.

Service Delivery

Wisconsin city and village municipal leaders were asked to evaluate a total of six service delivery improvement strategies (Table 3). The most frequently agreed with strategies include:

- improving productivity through better management (61.1 percent);
- pursuing regional cooperative agreements (48.3 percent); and
- contracting out services (44.9 percent)

A clear majority thought that improved productivity through better management was a viable strategy. Surprisingly, 17.2 percent of the respondents "strongly disagreed" with this approach as a viable strategy to reduce fiscal stress. Why there would such a strong dislike of this seemingly common sense approach is unclear and may warrant further investigation.

The strategies least supported by municipal officials were:

- the reduction of hours for public facilities (32.7 percent agreed or strongly agreed);
- department consolidation (36.5 percent); and
- service elimination (38.4 percent)

Revenue Strategies

When asked about the revenue side of the equation, there seems to be strong agreement that municipalities should adopt of *increase user fees and charges and pursue additional grants* from state and local government. Here 61.7 and 65.3 percent, respectively, supported these two ways to enhance revenues during times of fiscal stress. Slightly more than half (50.6%) of Wisconsin city and village officials responding to the survey believe that raising property taxes is a viable option. Drawing down cash reserves had a mixed reaction where 39.5 percent supported the approach, and one in ten strongly supporting the idea, was counter-balanced with 43.9 percent not agreeing with this particular strategy. The two options with the strongest options

include adopting or increasing user fees and charges with 19.7 percent strongly disagreeing and the pursuit of grants from higher levels of government with 19.5 percent strongly disagreeing.

Expenditure Strategies

The most frequently agreed with expenditure strategies include:

- targeted budget cuts (56.1 percent agreed or strongly agreed);
- delayed capital expenditures (55.4 percent);
- refinancing outstanding debt (50.3 percent); and
- delaying routine maintenance (42.9 percent).

The least agreed with expenditure strategies include:

- across the board budget cuts (34.6 percent agree or strongly agree);
- laying off workers (34.8 percent);
- discouraging population growth (35.1 percent); and
- increasing short-term debt (35.2 percent).

Strategies to reduce expenditures exhibit the greatest degree of divergence in the opinions of these local officials. Consider for example the option to refinance outstanding debt to secure better interest and payment schedules. A slight majority, 50.3 percent, supports this option, but 24.8 percent strongly disagreed. It may be the case that many municipalities have already taken advantage of historically low interest rates and it is widely expected that interest rates will increase. Indeed, the record low rates may explain the popularity of increasing short-term debt. Although only 35.2 percent of respondents support this idea, 17.6 percent strongly favor this option. Delayed capital expenditures as a solution also proves to be controversial. While 42.9 percent generally support delayed capital expenditures, 15.9 strongly disagree. The competing strategies of across the board budget cuts compared to targeted cuts also appear to be controversial. While a clear majority (56.1%) prefer targeted cuts and only 34.6 percent prefer across the board cuts, nearly one in five (17.4%) strongly disagree with the targeted cut approach.

Perhaps the most contentious finding is the strong support for discouraging population growth as a means to keep downward pressure on expenditures. While only 35.1 percent support this idea, 32.5 percent strongly supports this strategy. Interestingly, no respondents strongly disagreed with discouraging population growth as a fiscal stress reduction strategy. This result is particularly interesting because it puts a spotlight on the potential conflict that may arise within communities that are struggling with fiscal stress while at the same time promoting economic growth and development. Traditionally, local communities have often pursued economic growth and development as a way of expanding the tax base, hence reducing fiscal stress. Unfortunately, there is little research that supports this strategy. Rather, these survey results suggest that local officials understand that with economic growth and development there are increased demands placed on local services. Officials are beginning to realize that there is a delicate balance between enhanced revenues coming from growth and development and the new demands on services that will result.[3]

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[3] This result casts doubt on the logic of the Taxpayers' Bill of Rights (TABOR) as an economic growth and development policy. Proponents of TABOR argue that taxes in Wisconsin are out of proportion to income and act as a barrier to economic growth and development. If TABOR places downward pressure on the growth in taxes, then economic growth and development will be spurred. But, TABOR will create significant fiscal stress for most municipalities. The result here is that municipal officials may actively discourage growth as a means to minimize fiscal stress. TABOR may have unanticipated consequences on growth and development when viewed at the local level.

In addition to asking each respondent to assess the viability of each of the 20 identified fiscal stress alleviation strategies (Table 3), we also asked respondents to rank the "top five" strategies that they have or are considering pursuing. These results are reported in Tables 4 and 5. Consider first the most frequently identified strategies (Table 5). Of the 155 respondents, 100 (63.3%) identified the adoption or increase in user fees and charges as the preferred strategy followed by refinancing of outstanding debt (60.1%), delayed capital expenditures (55.7%), improved productivity through better management (54.4%), pursuit of grants from state or federal government and targeted budget cuts (both at 53.2%) and raising the property tax levy (52.5%). The remaining strategies were identified in the top five by less than 50 percent of the respondents. The least popular strategies include increasing short-term debt (19.0%), laying off public employees (17.1%) and discouraging population growth (12.0%).[4]

If we examine the frequency of how the individual strategies are ranked within the top five, a clear picture of the most common strategies becomes available (Table 4). The strategy that was ranking as the top strategy by most local officials include improved productivity through better management (28.8%), the adoption or increase in user fees and charges (17.9%), refinancing outstanding debt (14.1%), delayed capital expenditures (14.1%), pursuit of grants (13.5%) and the contracting out of services (10.3%).

Strategies for Fiscal Health

What are some strategies that local officials can think about to when considering options to create an environment for a stronger fiscal health position? Eight broad based strategies include:

1. Be more efficient in the production of services;
2. Expand the tax base;
3. Reduce the demand for services;
4. Shift costs to non-residents;
5. Secure new sources of revenue;
6. Increase spending flexibility;
7. Improve management of existing resources; and
8. Diversify revenue sources.

Note that none of these can be described as "quick fixes," rather these are long term strategies for long term fiscal health. Short-term quick fixes such as across the board reductions in expenditures or deferment of capital improvements or maintenance or exacerbates the long term viability of local governments. For example, for smaller more rural community expenditures on local roads is often the single largest expenditure category. A common fiscal crisis "solution" is to delay maintenance expenditures. Engineering studies have consistently documented that such strategies lead to a deterioration of roads and larger costs long term.

Vibrant communities that are socially and economically dynamic know that there are no quick fixes or simple solutions to complex problems. During times of fiscal stress, these same communities must look to long term solutions and seek opportunities to implement sound long term fiscal planning and fiscal health strategies. The interplay between the public and private sectors of the local economy are becoming more blurred as opposed to distinguished and well defined.

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[4] The last result may appear to be inconsistent with the arguments laid out in footnote two above. This is not the case. The results for discouraging population growth in Table 3 suggests that local officials have seriously thought about this as an option, but the results in Table 4 and 5 suggest that there are other strategies that officials would prefer to follow before discouraging population growth.

Local officials and concerned citizens should look upon the current fiscal situation as an opportunity for change rather than a crisis that requires quick answers. Political historians have documented that "radical" long term changes that have proven to be the foundation of sound public policy come out of time of crisis. It is almost human nature to be reactive to crisis then proactive, particularly in a political setting. Perhaps the current fiscal crisis is a window of opportunity for innovative communities to make significant strides forward. The future of the local economy may depend upon it.

References

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Table 1: Overall levels of Wisconsin city and village fiscal conditions.

	Current Condition	Condition in Five Years
Adequate revenues and able to reduce taxes.	4.5%	3.8%
Adequate revenues but not able to expand services	41.9	37.6
Inadequate revenues but not reducing services	29.7	22.9
Inadequate revenues and reducing services	23.9	35.7
sample size: 155		

University of Wisconsin Survey, 2004

Table 2: Specific measures of Wisconsin city and village fiscal conditions

	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
Our current fiscal situation is acceptable	8.4%	36.1%	21.3%	23.9%	8.4%
We are able to maintain three months of operating expenditures with current cash reserves	3.2	49.0	7.7	9.7	30.3
Our current capital improvement plan is fully financed	17.1	20.4	19.1	33.5	9.9
Our current credit rating is acceptable	0.0	47.7	14.8	5.8	31.6
We are near our debt level capacity	25.5	15.3	10.8	40.1	8.3
We have been able to roll over cash reserves from the previous budget cycle	3.9	49.7	14.8	14.8	16.8
We are faced with unfunded pension responsibilities	24.5	20.6	12.3	29.7	12.9
We are able to maintain our current employee benefits package	7.7	30.3	24.5	29.0	8.4
sample size: 155					

University of Wisconsin Survey, 2004

Table 3: Levels of support for specific strategies in response to fiscal stress

	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
			Service Delivery		
Improved productivity through better management	3.8%	57.3%	18.5%	3.2%	17.2%
Contracted out services	5.7	39.2	25.9	22.1	6.9
Consolidated departments	10.9	25.6	26.9	32.0	4.5
Pursued regional cooperative agreements	3.9	44.4	26.8	15.7	9.1
Reduced hours for public facilities	10.3	22.4	21.1	42.9	3.2
Eliminated services	9.6	28.8	18.6	37.8	5.1
			Revenues		
Drawn down cash reserves to meet daily operations	10.2%	29.3%	16.5%	38.2%	5.7%
Raised property tax levies	8.8	41.8	15.2	25.9	8.2
Adopted or increase user fees and charges	2.5	59.2	9.5	8.9	19.7
Created or expanded enterprise funds	3.2	25.3	40.3	26.0	5.2
Pursued grants from federal/state government	0.0	65.3	8.4	6.5	19.5
			Expenses		
Refinanced outstanding debt	5.1%	45.2%	11.5%	13.8%	24.8%
Increased short-term debt	17.6	17.6	22.2	38.7	3.9
Delayed routine maintenance expenditures	5.1	37.8	16	30.8	10.3
Delayed capital expenditures	3.2	52.2	10.2	18.5	15.9
Laid off workers	20.6	14.2	14.8	45.8	4.5
Hiring freeze	9.7	27.7	28.4	25.8	8.4
Across the broad budget cuts	6.4	28.2	23.1	31.4	10.9
Targeted budget cuts	1.9	54.2	12.9	13.5	17.4
Discouraged population growth	32.5	2.6	14.3	50.6	0
sample size: 155					

University of Wisconsin Survey, 2004

Table 4: Ranking top five strategies in response to fiscal stress

	Ranked #1	Ranked #2	Ranked #3	Ranked #4	Ranked #5	Not selected
			Management			
Improved productivity through better management	28.8%	9.0%	5.8%	4.5%	7.1%	44.9%
Contracted out services	10.3	11.5	3.8	7.7	5.8	60.9
Consolidated departments	5.1	5.8	7.7	3.2	8.3	69.9
Pursued regional cooperative agreements	5.8	9.6	12.2	7.1	7.7	57.7
Reduced hours for public facilities	3.2	3.8	3.8	4.5	8.3	76.3
Eliminated services	7.1	5.1	8.3	4.5	12.2	62.8
			Revenues			
Drawn down cash reserves to meet daily operations	8.3%	7.7%	8.3%	9.0%	5.8%	60.9%
Raised property tax levies	9.0	11.5	9.6	6.4	16.7	46.8
Adopted or increase user fees and charges	17.9	16.7	15.4	5.8	8.3	35.9
Created or expanded enterprise funds	2.6	5.1	11.5	6.4	9.0	65.4
Pursued grants from federal/state government	13.5	14.7	10.3	8.3	7.1	46.2
			Expenses			
Refinanced outstanding debt	14.1%	13.5%	7.1%	17.3%	9.0%	39.1%
Increased short-term debt	1.3	1.3	3.8	7.7	5.1	80.8
Delayed routine maintenance expenditures	1.9	10.3	9.0	8.3	7.1	63.5
Delayed capital expenditures	14.1	11.5	11.5	8.3	10.9	43.6
Laid off workers	1.9	3.8	1.9	1.9	7.7	82.7
Hiring freeze	1.9	3.8	5.8	1.3	11.5	75.6
Across the broad budget cuts	10.3	6.4	7.7	4.5	9.0	62.2
Targeted budget cuts	9.6	12.8	10.9	11.5	9.0	46.2
Discouraged population growth	1.3	0.0	1.3	0.6	9.0	87.8
sample size: 155						

University of Wisconsin Survey, 2004

Table 5: Most frequently identified strategy

	Number in top 5	
Adopted or increase user fees and charges	100	63.3%
Refinanced outstanding debt	95	60.1%
Delayed capital expenditures	88	55.7%
Improved productivity through better management	86	54.4%
Pursued grants from federal/state government	84	53.2%
Targeted budget cuts	84	53.2%
Raised property tax levies	83	52.5%
Pursued regional cooperative agreements	66	41.8%
Contracted out services	61	38.6%
Drawn down cash reserves to meet daily operations	61	38.6%
Across the broad budget cuts	59	37.3%
Eliminated services	58	36.7%
Delayed routine maintenance expenditures	57	36.1%
Created or expanded enterprise funds	54	34.2%
Consolidated departments	47	29.7%
Hiring freeze	38	24.1%
Reduced hours for public facilities	37	23.4%
Increased short-term debt	30	19.0%
Laid off workers	27	17.1%
Discouraged population growth	19	12.0%

University of Wisconsin Survey, 2004