Georgia Journal of Public Policy

Volume 1 | Issue 1 Article 3

March 2011

Impact of the Economic Downturn on Local Governments in South Carolina

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Introduction

Across the country local government revenues have decreased while operating costs such as fuel, materials, equipment, and health insurance costs have significantly increased. In addition to reduced revenues, interest earnings for city and county government investments are low. These factors combined have created a difficult financial arena in which local governments must operate. While economists are reporting signs of economic recovery, many city and county budgets are just now feeling the full brunt of the economic downturn that began in 2008. On a daily basis, news media nationwide report local governments addressing budget deficits by cutting services, eliminating positions, or furloughing employees.

To study the effect of the recession on South Carolina's local governments, the University of South Carolina's Institute for Public Service and Policy Research (IPSPR) conducted a survey to determine the true impact on local government revenues and the fiscal strategies municipalities and counties have used to reduce expenditures. The purpose of this article is to summarize the survey results and to detail how local governments in South Carolina reacted to the economic downturn.

Methodology

IPSPR staff constructed a 39-item survey asking a wide range of questions regarding recent budget history, expenditure adjustments, and revenue changes in the past two years and the upcoming year. The survey was modeled after surveys of Georgia municipalities and counties conducted by Kennesaw State University. Many items also were similar to surveys conducted by the International City/County Management Association and the National League of Cities (NLC). The commonality of the survey items allows for national and cross-state comparisons. Several municipal and county finance professionals reviewed the survey and suggested revisions and additional questions.

All 46 South Carolina counties and 167 of South Carolina's 270 municipalities were selected to receive the survey. Cities and towns with less than five employees or below a population of 1,000 were not included in the survey. Respondents had a choice of completing a web-based survey or template survey that could be faxed or e-mailed. The South Carolina Association of Counties and the Municipal Association of South Carolina sent e-mails to the survey participants explaining the purpose of the survey and encouraging their participation. ISPR staff followed up with an e-mail with the survey template and a link to the web survey. Follow-up e-mails were sent to participants who did not respond to the initial survey.

Response Rate

Forty municipalities responded to the survey, yielding a response rate of 24%. Smaller municipalities with less than 10,000 residents are underrepresented in the survey results as more than half of cities with populations greater than 10,000 responded to the survey. The 24% response rate was lower than the NLC survey response rate of 36%[1] and the Kennesaw State study response rate of 43%[2].

Twenty-one counties responded to the survey, for a response rate of 46%. Similar to the municipal results, the smaller counties are underrepresented, as two-thirds of the counties with populations greater than 100,000 responded to the survey. The Kennesaw State study response rate was 66%[3].

Profile Information

The majority of the cities and towns that responded to the survey are full service jurisdictions (see Table 1). The average FY10 general fund budget for the responding jurisdictions was $17,882,957 with a range of $455,800 to $125,500,000. The average number of FTE (full time equivalent) positions in FY10 for those responding was 229 with a range of 10 to 1,691.

TABLE 1

Service Provided	Number	Percentage
Police	40	100
Business License	40	100
Sanitation	38	95
Fire	36	90
Codes Enforcement	35	88
Water	26	65
Sewer	26	65
Electric	8	20

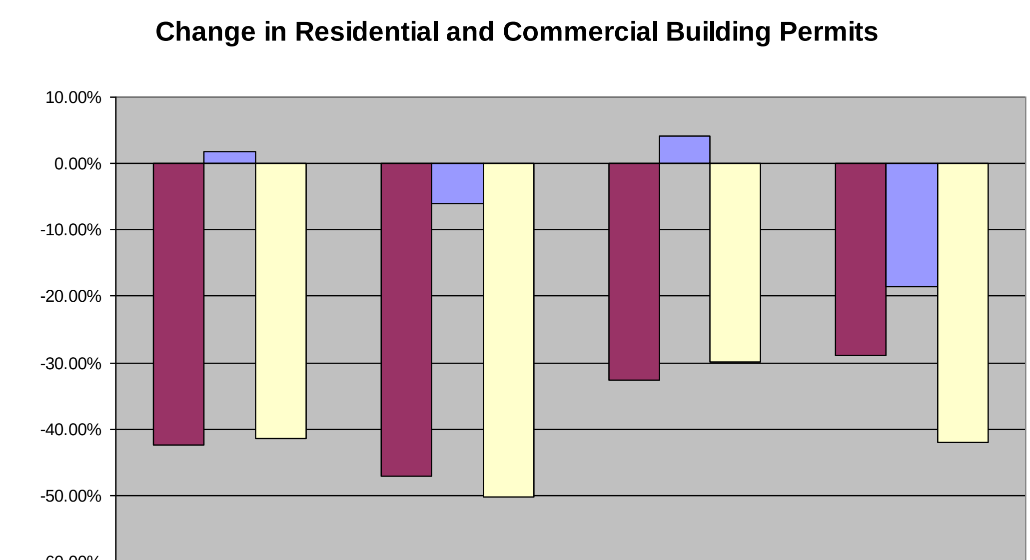
In general, counties in South Carolina provide the same core services, including law enforcement and court functions, emergency medical services, road maintenance, and tax assessments and collections. The average FY general fund budget for the responding counties was $63,031,659 with a range of $8,246,614 to $167,452,393. The average number of FTE positions in FY10 was 870 with a range of 112 to 2,236.

[1] Hoene & Pagano, 2009
[2] Burruss, 2010a
[3] Burruss, 2010b

State of Local Government Revenues

It should come as no surprise that there has been a decline in most local government revenue categories over the past two years. High unemployment and the struggling real estate market have resulted in reduced consumer spending and fewer business transactions with municipal and county governments. A prime example is the significant decline in the number of commercial and residential building permits for new construction in the past two years.

FIGURE 1



	Municipal Residential	County Residential	Municipal Commercial	County Commercial
2008-2009	-42.43%	-47.06%	-32.57%	-28.95%
2009-2010	1.83%	-6.08%	4.06%	-18.46%
2008-2010	-41.38%	-50.28%	-29.83%	-42.06%

Fifty percent of those responding to the surveys indicated they have had at least one large employer in the community either close or significantly reduce its workforce in the last two years. Reduced local government revenues usually means less local government spending, which also has a negative impact on the economy of the local community[4].

[4] Alliance for Innovation, 2009

The following is a summary of the estimated revenue change in several general fund revenue categories for the municipalities responding to the survey:

TABLE 2
Local Government Revenues

Revenue Category	% Change from FY08 to FY10	
	Cities	Counties
Property Tax	5.4	11.3
Local Option Sales Tax	-39.8	-14.1
Permit Fees	-27.7	-47.9
Business Licenses	-9.1	-19.7
Fines/Forfeitures	-9.1	-10.5
User Fees/Charges	-3.1	-9.8
Other Fees/Taxes	10.1*	9.8*
Franchise Fees	19.8*	-13.3

***Increase mostly due to addition of new fees or increase in existing fees/taxes**

In addition, state aid to municipal subdivisions has been cut 18.8% since FY08 and other municipal revenue sources such as hospitality taxes (-8.3%), and accommodations taxes (-16.4%), also have declined in the past two fiscal years. Similar to the situation in municipalities, state aid to subdivisions for counties has been cut 18% since FY08 and other revenue sources such as hospitality taxes (-4.6%)s and accommodations taxes (-20.3%), also declined in the past two fiscal years.

For most local governments in South Carolina, the largest portion of general fund revenues comes from property taxes. The impact of the decline in the real estate market over the past two years is becoming apparent in property tax revenues. In FY10, 78% of the municipal respondents and 83% of the county respondents either had predicted a decrease in property tax revenue or a smaller increase compared to FY09. As lower home values impact reassessments over the next few years, property tax revenues also are likely to be lower[5].

Since the inception of state mandated limits on local governments' ability to raise property taxes, some local governments have raised property taxes a small amount each year. However, with a negative change in the CPI, municipalities and counties in South Carolina with no population growth are prohibited from raising taxes. In FY09, 36% of the municipal survey respondents and 47% of the county survey respondents raised property taxes. For FY10, 28% of the municipalities and 41% of the counties reported an increase or an intention to increase property taxes. In comparison, municipalities and counties in Georgia have been less likely to raise taxes. In the Kennesaw State study[6], 12% of municipalities and 23% of counties reported raising property taxes in FY09 and only 6% of municipalities and 8% of counties planned to increase property taxes in FY10.

Twenty percent of municipalities reported instituting new fees over the past two years, while 35% increased existing fees. The most common fee initiated or increased was solid waste collection, followed by utility fees (electric, water/sewer or stormwater), franchise fees, and

[5] Hoene & Pagano, 2009
[6] Burruss, 2010a,b

recreation fees. For counties in South Carolina, 26% of the survey respondents reported instituting new fees over the past two years, while 72% increased existing fees. The most common fee increased was for emergency management services.

Local Government Expenditures

Overall, the general fund budgets of the responding cities and towns have remained relatively flat over the last two years with a 1.1% increase from FY08 to FY10. Fifty-three percent of the responding jurisdictions had a decrease in their general fund budgets for FY10. According to the Kennesaw State study[7], 68% of Georgia municipalities had a decrease for this same period. For counties in South Carolina, the general fund budgets increased 2.2% over the past two years and 63% of the respondents reported a decrease in their general fund budgets for FY10. In Georgia, 89% of the counties surveyed reported a budget decrease for FY10[8].

Thirty percent of municipal respondents indicated they have reduced or eliminated services during the current fiscal year or past fiscal year as a result of the downturn in the economy. Respondents were asked to specify the services that were impacted. The most common response was changes to or elimination of sanitation services. Thirty-three percent of South Carolina counties reported having reduced or eliminated services. The most frequent service mentioned as being impacted was maintenance to county roads.

As mentioned previously, there have been reductions in state aid to subdivisions over the past few years. Depending on the size of the local government and the size of the budget, this revenue source may constitute a significant portion of the budget. Respondents were asked to report the impacts directly related to the reductions in state aid to subdivisions. The following table lists the most common responses. Fifteen percent of the municipal respondents and 5% of the county respondents indicated the cuts in the state aid to subdivisions have not yet impacted staff, budgets or service delivery.

TABLE 3

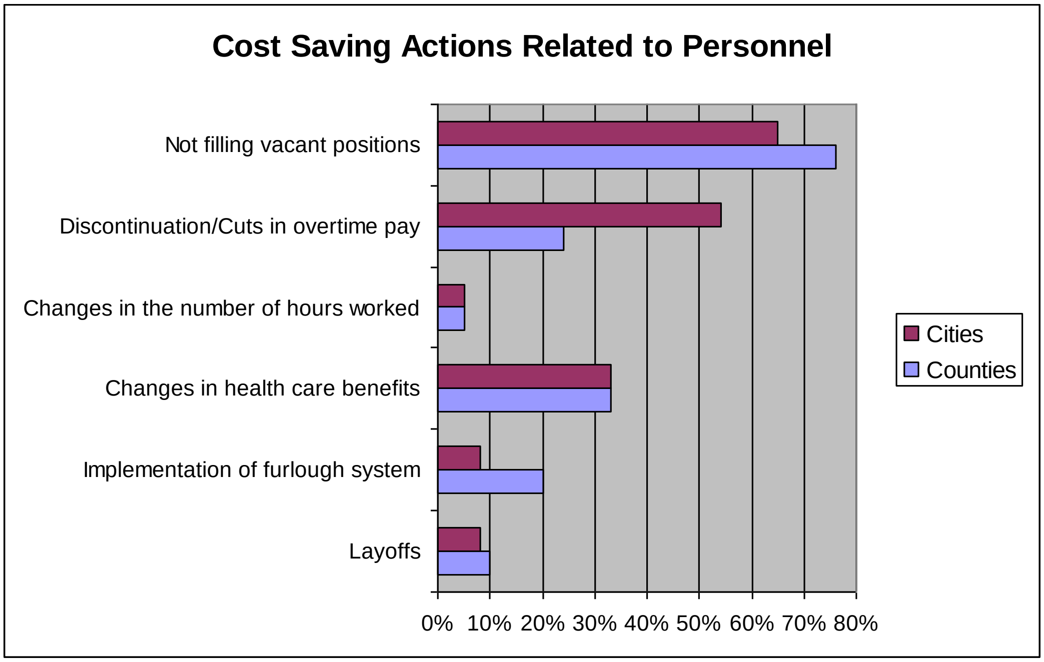
Impact of Decline in State Aid to Subdivision	**Municipalities**		**Counties**	
	Number	**Percentage**	**Number**	**Percentage**
Personnel impacts (layoffs, furloughs, hiring freezes, etc.)	8	20	9	42.9
Reductions in overall operating expenses	5	12.5	4	19.1
Delays in capital purchases/projects	4	10	7	33.3
Use of unreserved fund balances	3	7.5	4	19.1
Increase in fees/taxes	1	2.5	1	4.8
Reduction in funding to outside agencies	0	0	3	14.3

[7] Burruss, 2010a
[8] Burruss, 2010b

Cost Savings Actions Related to Personnel

Personnel costs are a significant portion of any local government's budget and are typically impacted in times of fiscal stress. As illustrated in the survey data in Figure 2, jurisdictions tend to take actions that minimize the negative impact on current employees. Layoffs, furloughs and reduced work hours are used less often than other actions for reducing personnel costs.

FIGURE 2



The results are similar in Georgia. According to the Kennesaw State study, reducing work hours, layoffs and furloughs were the least frequent personnel actions taken by Georgia cities and counties as cost savings measures[9].

Another method local governments have used to reduce expenditures is not giving employee raises. In those jurisdictions that responded to the survey, there was a substantial reduction in the number of jurisdictions giving employee raises from FY09 to FY10.

TABLE 4

	Percentage Giving Employee Raises	
	FY09	**FY10**
Cities	59%	29%
Counties	86%	15%

In addition to personnel reductions, there are common cutback management techniques that local governments employ. The most common areas cut since FY08 are reported in Figure 7:

[9] Burruss, 2010a,b

TABLE 5				
Areas Cut Since FY08	**Cities**		**Counties**	
	Number	Percentage	Number	Percentage
Travel	35	88	17	81
Equipment	32	80	16	76
Training	30	75	17	81
Supplies	27	68	11	52

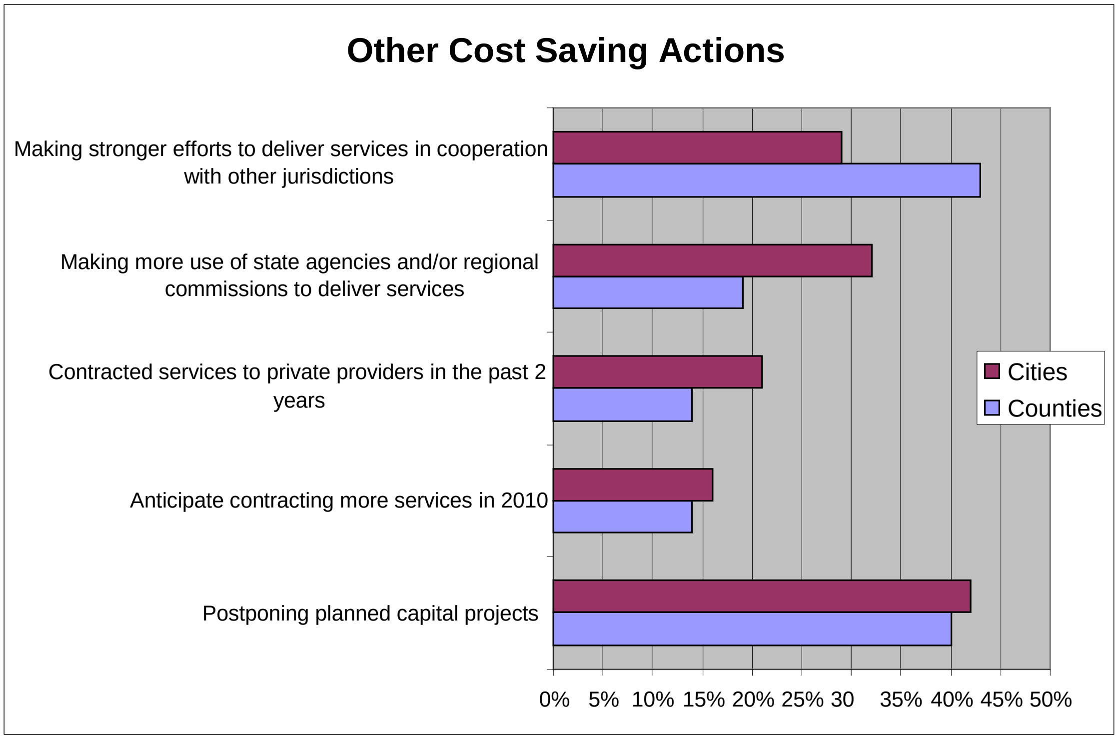
Forty percent of municipalities and 30% of counties indicated cancelling or postponing planned capital projects in FY09. A larger number (43% of municipalities and 40% of counties) reported cancelling or postponing planned capital projects in FY10. This was less than the 62% reported in the National League of Cities' *City Fiscal Conditions 2009 Report*. One could argue that delaying capital projects is fiscally responsible in the short-term. However, local government leaders may realize the service implications of not funding capital projects and could take advantage of lower interest rates and more competitive bidding for completing these types of projects[10].

Other Cost Saving Measures

There are other strategies local governments can use to reduce costs in times of budgetary shortfalls. Based on the survey responses, most jurisdictions in South Carolina are more likely to seek grants and reduce funding. Other cost savings actions are displayed in Figure 3. In addition to these measures, about 40% of South Carolina jurisdictions indicated they have adopted energy savings programs in the past two years. Similar results were found in the Kennesaw State survey[11].

[10] Hoene & Pagano, 2009
[11] Burruss, 2010a,b

FIGURE 3



Reserve Fund

Most jurisdictions use the unrestricted fund balance in their general fund budget as a "rainy day fund." In fact, some local governments have a specific dollar amount or percentage designated by policy as a target for the unrestricted fund balance. The Government Finance Officers Association recommends that governments establish a formal policy and at a minimum maintain an unrestricted fund balance of no less than two months (16.7%) of general fund operating expenditures[12]. A summary of responses regarding fund balance policies is presented below:

TABLE 6

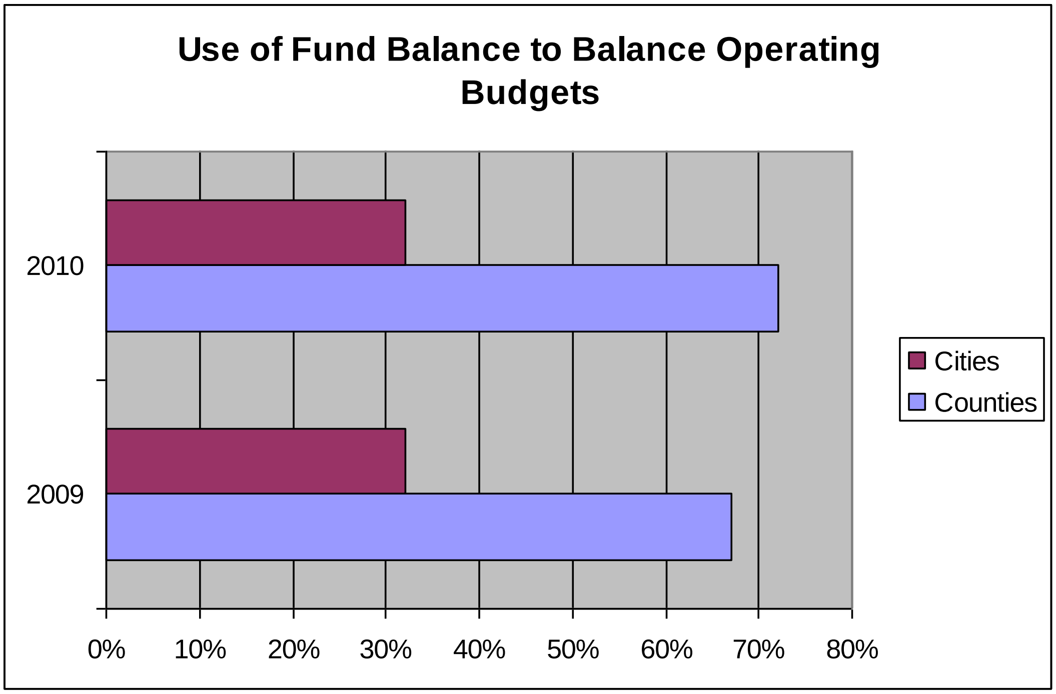
	Policy Target for Unrestricted Fund Balance	Actual Unrestricted Fund Balance
	Municipalities	
Average	24%	30.1%
Range	10% - 35%	1% - 70%
	Counties	
Average	19.1%	17.5%
Range	10% - 30%	6% - 58%

Since the economic downturn began in 2008, some local governments have had to use a portion of this fund to address budgetary shortfalls (see Figure 4). This was a more common

[12] GFOA, 2009

practice in South Carolina than it is in Georgia in 2009, with 26% of Georgia cities and 38% of Georgia counties using fund balances to balance operating budgets.

FIGURE 4



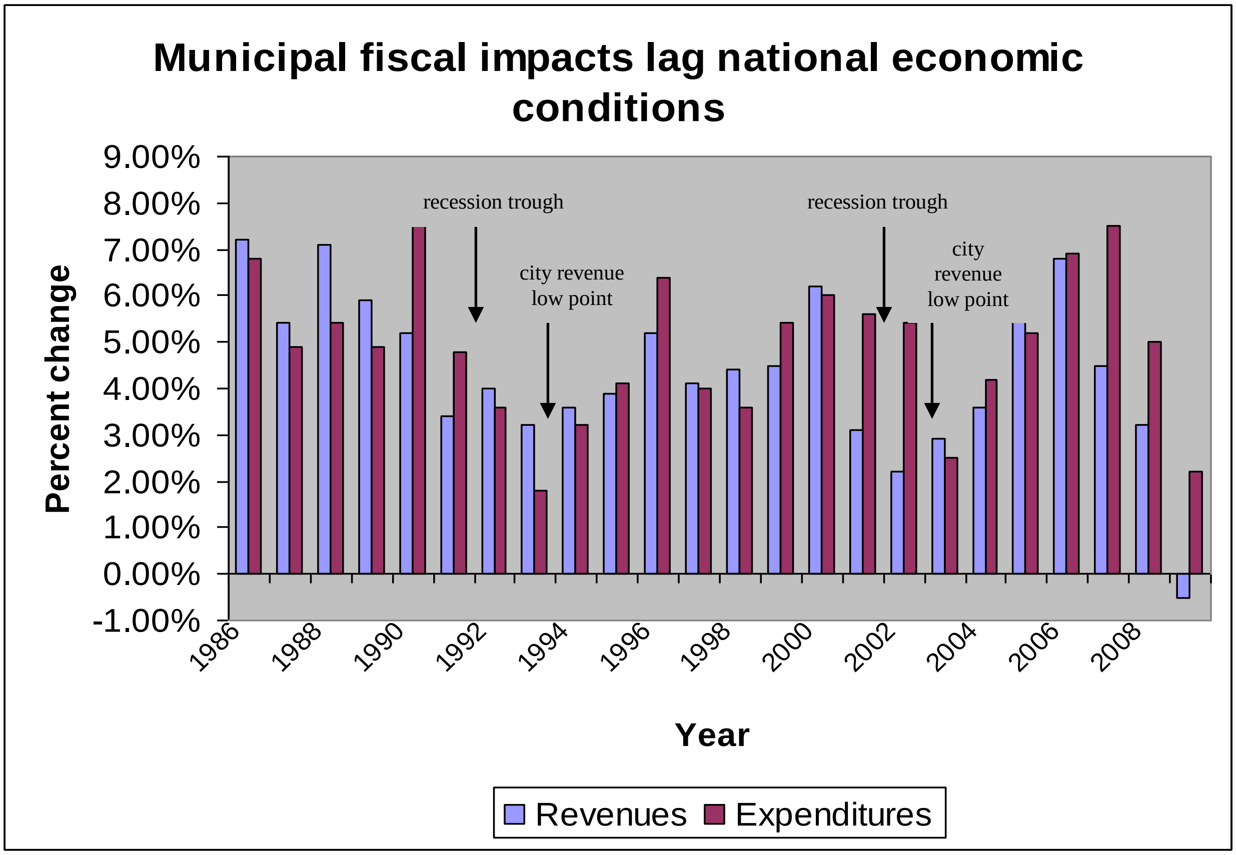
Conclusion

It is apparent that the current economic condition has caused local governments to implement a wide range of cutback measures. Options on the revenue side are limited – the ability to raise property taxes is limited and initiating new fees or increasing existing fees may not be acceptable to citizens or the city or county council.

There are signs of the beginning of national economic recovery. Even with the end of the recession, most experts believe it will take some time for local government revenues to stabilize[13]. Based on past recessions, that time period could be anywhere from 18 months to several years. The chart below illustrates the lag in municipal revenues in past recessions.

[13] Hoene & Pagano, 2009

FIGURE 5



As illustrated in these survey findings, most of the traditional coping mechanisms for addressing budgetary shortfalls have been employed. With projections of continued cuts in aid to local subdivisions and declining tax and fee revenues, the old adage of "doing more with less" is no longer possible. The current short-term impacts of the recession may become the normal operating conditions for the foreseeable future[14]. Local governments that continue to experience economic distress may be required to make difficult decisions regarding changes they have avoided in the past, such as eliminating employees and services, consolidating services, and partnering with other governments to provide services.

The Institute for Public Service and Policy Research plans to conduct a follow-up survey in 2011 to study continued impacts of the recession and what additional actions local governments have taken to address further budgetary shortfalls. The second phase of this research will analyze the longer term impact of this economic downturn on local government finances and services in comparison with other periods of economic stress over the last two decades. Researchers will examine if there is a differential impact on communities based on key demographic and economic variable profiles, and how these community factors have impacted local governments. The results of the project will highlight leading financial and budgetary practices from those jurisdictions that are minimally impacted and hopefully serve as a guide for local governments in the future.

[14] Purcell, 2009

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