THE WISCONSIN
TAXPAYER

Vol. 81, Number 4 | April 2013

The Local Squeeze?

State Aid Cuts, Tax Limits, and Local Government Finances

Since 1995, state shared revenues to municipalities and counties have been significantly reduced three times, leaving these aids below their 1990 levels. Those reductions, along with state-mandated property tax limits initiated in 2005-06, held the average growth in municipal and county revenues to less than 3% per year since then. With lagging revenues, local governments continued to fund public safety but slowed spending in other areas. They also continued to borrow, so debt service expenditures in annual budgets are growing quickly.

Like many individuals and businesses, municipalities and counties have faced increasing financial pressures over the past 15 years. Prolonged state budget difficulties, combined with changing state spending priorities, led to reduced state aid to local governments.

Funding challenges became more acute after 2005 when the state restricted annual increases in municipal and county property taxes. These caps (levy limits), combined with state aid cuts, slowed revenue growth for both municipalities and counties.

Local governments responded in at least two ways. First, they slowed overall spending to match available revenues. And second, they reexamined past spending trends and priorities. In general, counties and municipalities continued to fund critical services but scaled back expenditures in other areas.

STATE SQUEEZE

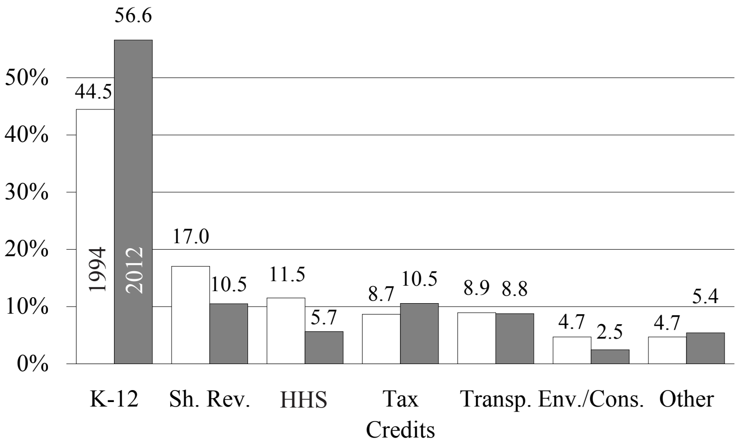
Wisconsin state government has long devoted a large share of its spending to aiding local governments—schools, municipalities, and counties, with K-12 schools receiving the most. However, over the past 15 years, changing priorities, slowing tax revenue, and persistent budget problems resulted in state government scaling back the share of its tax dollars going to municipalities and counties.

Local Assistance

The state provides several kinds of financial help to local governments. Shared revenues (now referred to as county and municipal aids) are unrestricted payments from the state that can be used to fund any local government service. Transportation aids help fund roads, bike paths, public transportation, and related spending. The state also assists counties in paying for human service programs.

During the first half of the 1990s, local assistance—aids to counties and municipalities, school aids, and reimbursement for credits on

Figure 1: K-12 School Aids Dominate Local Assistance Payments
State Aid to Local Gov'ts by Type, % of Total, 1994 and 2012



individual property tax bills—averaged 35% of total state government spending and 57% of its general fund spending. The general fund is the part of the state budget that is supported primarily by taxes on individual and corporate incomes, sales, tobacco, and alcohol. Remaining state expenditures are funded with segregated taxes (e.g., the state gas tax), fees and charges, and federal funds.

Aids to municipalities and counties averaged about 14% of all state spending during 1990-95; shared revenues averaged about 13% of general fund spending.

Changing State Priorities

After 1995, state spending priorities shifted, with aid to counties and municipalities negatively affected.

More Focus on School Aid. First, state lawmakers committed to providing "two-thirds" of K-12 school revenues beginning in 1996-97. To reach the two-thirds goal, they increased school aids 12.6% in 1995, 9.9% in 1996, and 31.8% in 1997.

With school costs rising, this two-thirds commitment required additional state taxes to be devoted to K-12 schools. As it became more and more difficult to meet, the state eliminated the two-thirds commitment in 2003. However, for several years thereafter, legislators tried to continue funding schools at the two-thirds level.

Figure 1 shows the impact of this priority shift. In 1994, school aids were 44.5% of all state assistance to local units; in 2012, they were 56.6% of the total. By contrast, shared revenues for municipalities and counties were 17.0% of all local assistance in 1994 but only 10.5% in 2012.

During 1995-2012, lawmakers also placed greater emphasis on property tax credits that benefit individuals rather than governments. Part of the "two-thirds" school funding commitment was a 1997 increase in school-related property tax credits. Those credits were again increased in 2007, 2008, and 2009. Another property tax credit (the First Dollar Credit) was added in 2009, and by 2012 it had more than doubled. In 1994, total property tax credits were about half of shared revenue payments; in 2012, the two were about equal.

Other Programs. State spending shifted outside of the local assistance programs as well. During the 1990s, corrections spending rose rapidly as the state built and filled prisons. In the 2000s, state funding for Medicaid rose faster, shifting tax dollars from local assistance to this jointly funded program (federal and state) for low-income residents.

BadgerCare, the state's primary Medicaid program, has been repeatedly expanded since its inception in 1999. In the early 2000s, lawmakers added SeniorCare, Wisconsin's prescription drug program. From 1999 through 2012, participation in Medicaid programs rose from 445,000 to 1.17 million, and total spending climbed from $2.6 billion to nearly $7 billion.

THE WISCONSIN

TAXPAYER

April 2013 Vol. 81 Number 4
Publication Number USPS 688-800
Periodical postage paid at Madison, Wisconsin

Subscription Price:
$17.97 per year
Published each month, except July, by the Wisconsin Taxpayers Alliance, 401 North Lawn Avenue, Madison, Wisconsin 53704-5033

Postmaster:
Send address changes to *The Wisconsin Taxpayer,*
401 North Lawn Avenue, Madison, Wisconsin 53704-5033
Phone: 608.241.9789 Fax: 608.241.5807
Email: wistax@wistax.org Website: www.wistax.org

Slowing Revenues

A second factor affecting aid to local governments was decelerating state tax revenues after 1999. Tax collections rose rapidly during the 1990s due primarily to a strong economy and a state income tax that was not indexed (adjusted for inflation). During 1990-99, income tax collections climbed an average of 7.8% per year; general fund tax collections rose an average of 6.5% per year. This growth was one reason the state was able to commit to two-thirds of school funding in 1997, fund prison expansion, and create BadgerCare in 1999.

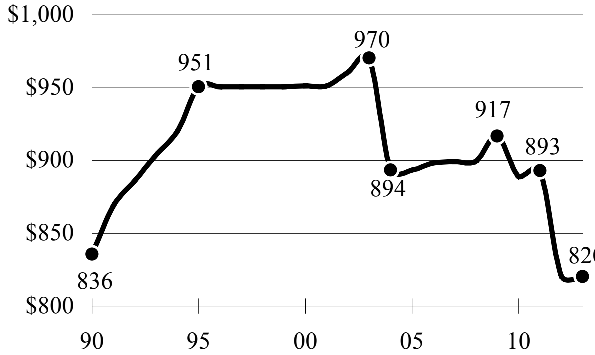
However, tax collections grew more slowly during 1999-2012, averaging only 2.4% per year. Three factors were primarily responsible. First, lawmakers indexed the state income tax beginning in 1999. With tax brackets and the standard deduction adjusted for inflation each year, collections slowed. Second, beginning in 2000, state income tax rates were lowered, temporarily reducing collections. And finally, recessions in 2001 and especially in 2008-09 reduced tax revenues.

Impact on Local Aids

As state revenues slowed and priorities shifted, the commitment to local assistance, particularly shared revenues, waned. Between 1990 and 1995, shared revenues rose nearly 14% from \$836 million to \$951 million (see Figure 2). However, they remained essentially unchanged over the ensuing six years, before increasing slightly in 2002 and 2003.

State budget problems led to a nearly 8% shared revenue cut in 2004. Continued state fiscal challenges meant little change through 2011, followed by another 8% cut in 2012. Multiple reductions over the past 10 years left 2013 shared revenues below their 1990 levels.

Figure 2: Shared Revenues Stall, Fall
County & Municipal Shared Revenues, 1990-2011, \$ Millions



Municipal Aid. Shared revenue cuts affected municipalities the most. About 80% of the shared revenue appropriation goes to cities, villages, and towns. Moreover, these aids account for more than 60% of total state aid to municipalities.

Multiple reductions in shared revenues over the past 10 years left the 2013 amount below the 1990 level.

The 20-year pattern of aid growth and decline makes clear the impact of the shared revenue cuts. After rising an average of 5.2% per year during 1990-95, total state aids to municipalities increased an average of only 1.4% per year during 1995-2003. During more recent years (2003-11), they changed little. After accounting for inflation and population changes, total state aids to municipalities fell more than 20% during 2003-11. Total aid figures for 2012 and 2013 are not yet available.

County Aid. Shared revenue cuts impacted counties less because these dollars account for only about 10% of their total state aid. Counties rely more on aids for health and human services and for transportation.

Total county aid increased an average of 7.3% annually during 1990-95. Average growth slowed to 3.2% during 1995-2003 and to 2.4% during 2003-08. Reduced state assistance for highways, health, and human services after 2008, along with shared revenue cuts, resulted in a 17% decline in total state aid to counties during 2008-11. Adjusted for population and inflation, the decline was over 20%.

LOCAL FUNDING SHIFTS

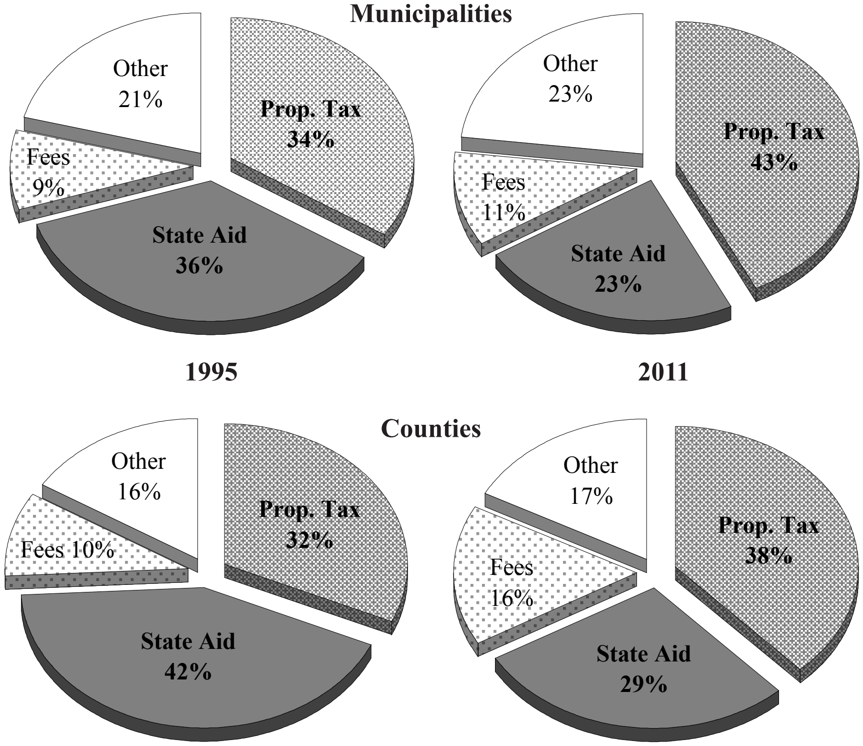
As state aid growth slowed and then declined, local governments compensated by raising property taxes and fees.

Municipalities

Under state law, municipalities have only one major tax available, the property tax. Cities, villages, and towns also can raise revenue via fees (such as those for garbage collection, recreation programs, park rental, and building permits) and fines. They also receive state and federal aid, but the amount is generally determined by state and federal officials.

During 1995-2011, state aids to municipalities rose a total of 11.8%, or less than 1% per year. With

Figure 3:
Property Taxes Support Rising Share of Municipal, County Services
Municipal and County General Revenues by Type, 1995 and 2011



limited aid growth, municipalities shifted the funding of local services to other revenues. As a result, municipal property taxes (+114.7%) and fees (+106.0%) more than doubled.

Figure 3 highlights the shift in funding. In 1995, 36% of municipal revenues were state aids; in 2011, 23% were. Property taxes climbed from 34% of municipal funding to 43%. Fees rose from 9% of revenues in 1995 to 11% in 2011.

Counties

The general pattern for counties was similar. State aids increased 20.7% during 1995-2011. County property taxes climbed 114.1%, and fees were up 195.5% during this period.

The bottom half of Figure 3 shows the change in how county services are paid for. State aid comprised 42% of county revenues in 1995 but only 29% in 2011. Property taxes rose from 32% to 38% of revenues, while fees jumped from 10% to 16%.

PROPERTY TAX LIMITS

As aid growth stagnated after 1995, municipalities and counties funded local services increasingly with property taxes. From 1995 through 2005, annual property tax growth averaged 5.7% in municipalities and 5.9% in counties.

In response to these increases, state lawmakers imposed levy limits on municipalities and counties beginning in 2006. Property tax increases were limited, with certain exceptions, to the higher of net new construction or a set percentage, initially 2% for 2006 and 2007. The percentage has since varied from just under 4% (2008) to 0% (2012 and 2013).

The tax limits slowed property tax growth. During 2005-2011, annual increases averaged 3.7% in municipalities and 3.2% in counties, two or more percentage points below the increases in the prior decade.

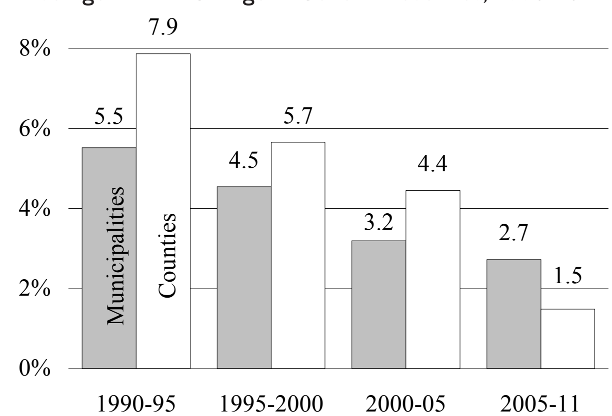
Total Revenues Slow

The combination of state aid and property taxes comprise the majority of local government revenues. When state aid increases little and property taxes are limited, total revenues for municipal and county governments rise slowly.

Municipalities. During 1990-95, municipal revenues rose an average of 5.5% per year. Increases slowed in each of the two subsequent five-year periods (see Figure 4). Revenue growth slowed further during 2005-11, averaging 2.7% annually.

Counties. County revenues followed a similar pattern. After rising nearly 8% per year during the first half of the 1990s, revenue increases slowed during each of the subsequent periods. A relatively large reduction in state aids slowed total revenue growth to an average of 1.5% per year during 2005-11.

Figure 4: Revenue Growth Slows
Average Annual Change in General Revenues, 1990-2011



SPENDING CHANGES FOLLOW

With revenue increases moderating over the past 16 years, local governments limited spending increases in many areas. Some municipalities also shifted expenditures from the general fund to other funds.

Total Spending

As expected, spending patterns for both municipalities and counties adjusted to revenue patterns.

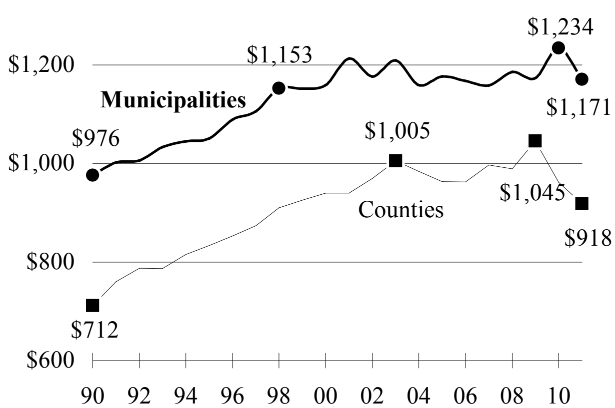
Municipalities. For cities, villages, and towns, average annual spending increases generally followed the revenue pattern illustrated in Figure 4 (page 4). They dropped from 5.5% during 1990-95 to 1.7% during 2005-11.

However, after accounting for inflation and population growth, municipal spending changed little since the late 1990s. In 2011, municipalities spent $1,171 per capita (see Figure 5), or about 2% more than the inflation-adjusted $1,153 spent in 1998.

While revenue changes explain much of these spending trends, accounting shifts also played a role. This study focuses on general fund spending, but municipalities and counties also have other funds which are used to account for enterprise activities, such as golf courses, electric utilities, and airports.

As state aids and property taxes moderated, some municipalities shifted spending from their tax- and aid-based general fund to fee-based proprietary funds. For example, some cities and villages created storm-water utilities that charge property owners a fee based on the size and characteristics of their property. The revenue is then used to maintain or upgrade municipal storm sewers. Creating a storm-water utility or shifting other spending to proprietary funds allows local governments to continue providing certain services, but it can also make it appear as though spending has slowed more than it has.

Figure 5: Municipal Spending Shifts
Cumulative Spending Growth Since 1990, General and Proprietary Funds, 1990-2011



Counties. Similar to municipal expenditures, county general fund spending paralleled revenue growth. During 1990-95, annual spending increases averaged 7.3%. Ten years later (2000-05), they averaged only 4.1%. Total county spending was up, on average, only 1.9% annually during 2005-11. For counties, there appears to be a little, if any, shifting of spending from the general fund to proprietary funds.

When inflation and population are accounted for, total municipal spending in 2011 was about 2% higher than in 1998.

Municipal Spending by Area

In addition to slowing overall expenditure growth, municipalities and counties altered priorities as well.

Public Safety. A significant share of municipal spending is for public safety—police, fire, and ambulance services. This is particularly true in cities, where it averages about 40% of spending (excluding debt service). It is less in villages (about one-third of spending) and towns (20%). Across all municipalities, public safety expenditures averaged 37.3% of spending in 2011.

Municipalities appear to have kept public safety a priority during the past 11 years. Total municipal spending climbed 28.8% during 2000-11, while public safety spending rose 43.6%.

Transportation. Historically, more than one of every four municipal dollars was spent on transportation, with nearly all of that for building and maintaining streets or roads. However, that percentage fell over the past 11 years due partly to increased focus on public safety.

Between 1990 and 2000, transportation expenditures rose from 26.5% of municipal spending to 27.4%. By 2003, it had fallen to 25.2%, and in both 2010 and 2011, it was below 25%. During 2005-11, it increased a total of 3.6%, compared to 10.6% for all municipal spending.

The recent moderation in transportation spending was not due to lack of road maintenance. During 2005-11, maintenance expenditures rose faster than overall spending (13.8% vs. 10.6%). Road construction, however, stagnated. After increasing 15.5%

during 2000-05, spending for new streets and roads increased only 0.6% during 2005-11. The recent recession played a role. With the housing market down, fewer subdivisions, and hence fewer city streets, were built.

Sanitation. As revenues tightened, one area where municipalities cut general fund spending was sanitation (mostly garbage collection, recycling, and sewers). It comprised 9.9% of municipal spending in 1990, but only 7.3% in 2000 and 6.0% in 2011.

The drop was due to less general fund spending on sewers and water mains. In 2000, municipalities spent more than $113 million from their general funds in this area. In 2011, they spent only $71 million.

This is one area where the shift to proprietary funds was notable. As mentioned (page five), over the past nine years (or more), some cities and villages have created storm water utilities. Municipal financial reports shows 12 cities or villages reporting proprietary storm water spending in 2011 but not in 2003. The 2011 expenditures totaled about $7 million.

General Government. The cost of operating a municipality, including the board, council, administration, and business office, is categorized as general government. Over the past decade, these costs increased at about the same rate as total expenditures. General government costs were up 25.5% during 2000-11 and 10.0% during the more recent 2005-11. Both increases were slightly less than those for total spending excluding debt (28.8% and 10.6%, respectively).

Shifting Priorities. The overall change in spending priorities over the past 11 years is recapped in Figure 6. Public safety was the main beneficiary with its share of municipal expenditures rising from 33.4% to 37.3%. The only other major category with an increased share of spending was parks and recreation.

County Spending by Area

Municipalities spend tax dollars on a wide variety of services. Counties, on the other hand, focus on three areas: health and human services, public safety, and transportation. In 2011, these three accounted for more than 75% of county expenditures.

Health and Human Services. Of those three, health and human services (HHS) predominates, accounting for more than 40% of county spending. However, due partly to a change in how long-term care services were provided, HHS spending fell during 2007-11.

During 2000-07, HHS spending rose by more than half, significantly faster than total spending (37.0%). The increase was due largely to expansion of Medicaid, a federal-state program whose services are largely delivered by counties. However, when long-term care services, and the state dollars that fund them, moved from counties to managed care organizations, county HHS spending dropped 13.1% during 2007-11. Total county spending was largely unchanged.

Public Safety. The second-largest county outlay is for public safety, mainly sheriffs' departments and county jails. In 2011, public safety accounted for about 23% of county expenditures.

Public safety was a county priority during 2000-11, as these expenditures increased faster (56.9%)

Figure 6: Public Safety Spending a Municipal Priority . . .
Municipal Spending Shares, 2000 (gray) and 2011 (pattern)

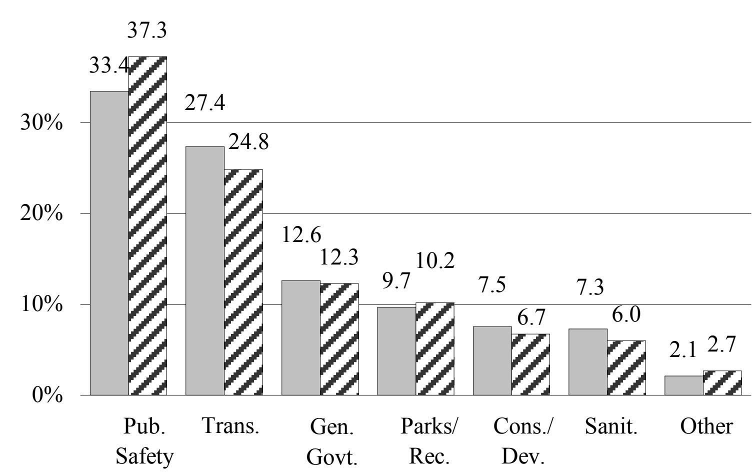


Figure 7: . . . And a County Priority
County Spending Shares, 2000 (gray) and 2011 (pattern)

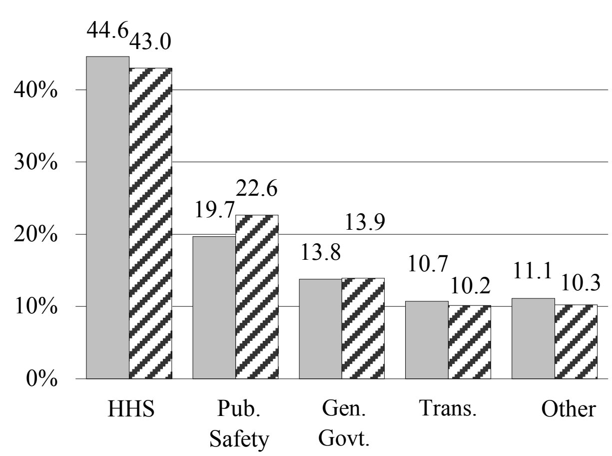
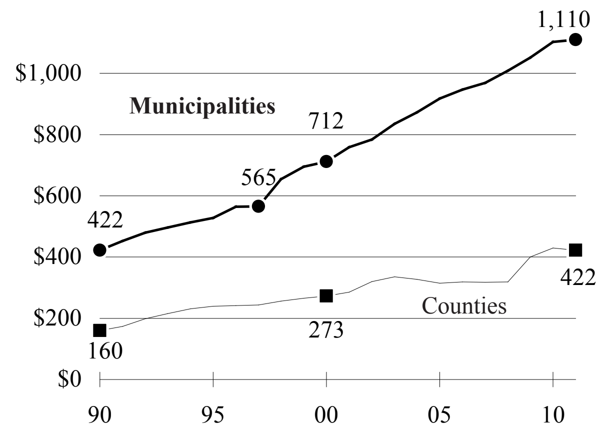


Figure 8: Per Capita Debt Climbs
Municipal and County General Obligation Debt Per Capita, 1990-2011



than those in any other major area. The county jail portion of public safety spending climbed over 60%.

Transportation. Just over 10% of county general spending is for transportation, much of it for road maintenance and repair. Transportation spending grew less (29.2%) than overall spending (36.6%) during 2000-11.

Spending Shifts. Due primarily to the decreases in HHS spending and increases in public safety, the composition of county spending has shifted since 2000. HHS spending dropped from 44.6% of spending in 2000 to 43.0% in 2011 (see Figure 7, page 6). Public safety spending rose nearly three percentage points to 22.6%. As a share of the total, expenditures on general government were about the same in 2000 and in 2011.

INCREASING DEBT & DEBT SERVICE

Despite, or maybe because of, smaller revenue increases, both municipalities and counties continued to accumulate long-term debt. As a result, annual debt service payments are rising.

Debt Rising, But At Slower Rate

Both county and municipal debt increased significantly during the 1990s. General obligation debt rose 85.3% in counties and 83.0% in municipalities; it more than doubled in towns (123.3%) and villages (109.9%), and it climbed 74.2% in cities. By comparison, state general obligation debt rose 53.6%; total state government debt climbed 80.0%.

During 2000-11, debt continued to grow but at a slower rate: 65.9% in counties and 67.2% in municipalities. However, local debt rose much less than state debt. State general obligation debt increased 135.6% and total state debt 163.6%.

There are several ways to compare debt levels over time. One is per capita. Figure 8 shows municipal debt rising from $422 per resident in 1990 to $1,110 in 2011. County debt increased from $160 to $422 per person.

A second way is based on property values. State law limits municipal and county debt to 5% of the total equalized (fair market) value of taxable property. The state ties debt levels to property values because property taxes are the prime source of local government revenue. Although a few municipalities are near their limit, as a whole, municipalities are well below the 5% cap. Total municipal debt equaled 1.3% of total statewide property value in 2011. Between 1990 and 2011, this percentage ranged from a low of 1.1% in 2007 to a high of 1.5% in 1992. County debt was significantly lower in 2011 at 0.5% of value.

Debt Service Growing

With both municipal and county debt rising, debt service—the annual interest payments plus charges for issuing new debt—also increased. In both cases, debt service payments rose faster than other expenditures.

Municipal debt service increased 41.5% during 2000-11, compared to 28.8% for other spending. County debt service rose 49.4% during these years, compared to 36.6% for everything else. With debt service growing faster than other spending, the risk is that these payments will increasingly "crowd out" other expenditures.

LOOKING AHEAD

The proposed 2013-15 state budget leaves shared revenues essentially unchanged. Like the 2011-13 state budget, the 2013-15 version retains strict municipal and county levy limits. Unless changed, property tax levies will be capped at the rate of new construction but not less than 0%.

With state aid stagnant and state levy limits tight, municipalities and counties will continue having to make hard program choices. However, 2011 Act 10's removal of benefits from collective bargaining and requirement that employees pay half of the total retirement contribution is generating savings, at least in 2012 and 2013. ☐

DATA SOURCES:
WISTAX calculations of Wisconsin Department of Revenue data.

wistax

Wisconsin Taxpayers Alliance

401 North Lawn Avenue • Madison, WI 53704-5033
608.241.9789 • www.wistax.org

PERIODICALS
USPS 688-800

WISTAX NOTES

■ **Federal Financial Assistance.** Wisconsin state government administered $12.9 billion in federal assistance in 2011-12, according to the state's Legislative Audit Bureau (LAB). Four areas comprised almost two-thirds of the total:

- $4.1 billion for Medicaid, the federal-state health program for low-income and disabled residents;
- $1.8 billion for federal unemployment benefits;
- $1.2 billion for the Supplemental Nutrition Assistance Program (SNAP, formerly called food stamps); and
- $1.2 billion for federal student financial aid.

As the chart (right) shows, federal assistance has been volatile over the past five years. In 2008, the state administered $10.0 billion in federal dollars. Due partly to federal stimulus spending (ARRA), federal money to the state jumped to $13.6 billion in 2009 and to $15.5 billion in 2010 when Wisconsin's share of stimulus spending peaked at $3.5 billion.

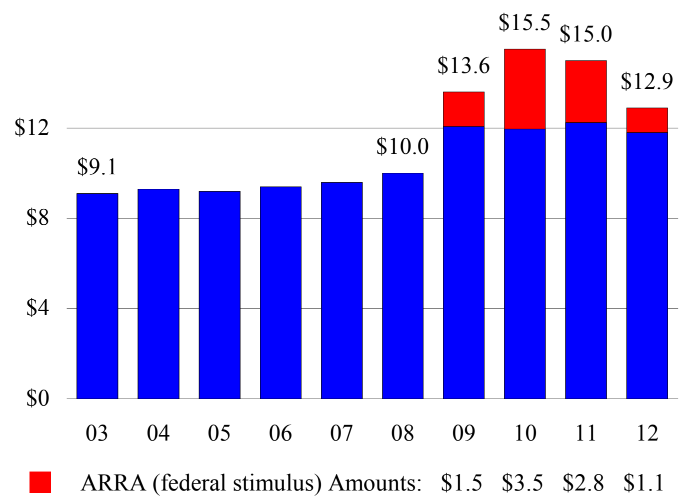
Total federal dollars have dropped in the past two years, as stimulus spending ebbed. Most of the 2012 ARRA funding was for enhanced or extended unemployment benefits.

Stimulus spending was only part of the reason for the jump of federal aid since 2008. Federal money for food stamps (SNAP) increased 176% from $442 million in 2008 to $1.2 billion in 2012. Federal unemployment benefits (+82%) and student financial aid (+71%) also rose significantly.

Areas with the smallest increases in federal assistance were federal dollars for highway planning and construction (+17%), research at the UW System (+20%), and K-12 special education (+22%).

According to the LAB, the 2012 total covers federal financial assistance for more than 2,000 federal programs and grants, including nearly 1,200 research and development grants to the UW System. Total federal assistance consisted of $11.5 billion in cash, $1.2 billion in noncash aid (e.g. food commodities), and $216 million in federal loan balances. ☐

Federal Financial Assistance Falls in 2012
Federal Funds Administered by State Agencies, 2003-12, ($ billions)



In FOCUS . . . recently in our biweekly newsletter

- Fiscal improvement, secure majorities lead to budget sticking points (I) (#4-13)
- State budget sticking points (II): Debt and deficits (#5-13)