

Local Budgets: An Uneven Squeeze

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Connecticut finished the last decade of the century in an enviable position. As we reported here in Spring 2003, state residents enjoyed the highest per capita income (\$28,766), the highest gross state product per non-farm worker (\$94,081), and the lowest unemployment rate (2.2%) in the nation in 2000. We also found, though, that the economic gains of the 1990s were unevenly shared by communities at different ends of the income spectrum. Connecticut's five richest towns registered stronger gains in per capita income and had a much better fiscal outlook than did the five poorest towns.

Unfortunately, the new decade began with a socioeconomic shock-wave—the terrorist attacks of 9/11—a recession, and a sluggish recovery that also have affected towns unevenly. Five years into the new decade, and facing renewed economic uncertainty, it seems a good time to monitor these changes. The additional motive for revisiting the rich town/poor town comparison is the widespread concern about the effects of federal and state budget shortfalls on local governments—the so-called "fiscal squeeze." Our central question: Has this downward fiscal pressure been evenly distributed, or has it widened the gap that we saw before?

PROPERTY TAX PRESSURE

The recession that officially bottomed out in late 2001 caused many state and local governments to rely more heavily on property taxes to finance local public spending. The *Wall Street Journal* reported (8/24/04,

p.1) that property taxes, as a share of total state and local revenues, rose to 28.2% in 2004-Q1, up from 25.5% in 2001-Q1—about 3 percentage points, but a 10.5% increase in the share over the three-year period. This increased reliance reverses a 1990s trend that saw property taxes shrink as a share of total state and local government revenues. Spurred by rapid growth of the high-tech and service sectors, the 1990s economic boom produced higher incomes—particularly from stock market capital gains—and boosted consumer spending. As a result, state coffers were awash in higher income tax and sales tax proceeds.

In Connecticut, the influx of income and sales tax revenues caused the property tax share of state and local revenues to fall more than 8% in the 1990s. Since the boom, however, Connecticut's reliance on property taxes has rapidly increased. Between fiscal years 2000 and 2002, property taxes rose from 20.1% to 23.5% of state and local revenues—an increase of 3.4 percentage points, but nearly a 17% increase in the share of revenues. Yet these overall figures mask the very different experiences of communities at the ends of the income distribution. Returning to the state's five richest and five poorest towns (measured by per capita income in 2000), the table illustrates the differential effects of the economic slowdown and subsequent "fiscal squeeze" on these ten communities.

LOCALIZED PAIN

New Canaan—the richest of the high-income towns—actually reduced its reliance on property taxes as a share of total revenues, by 1.9% between

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2000 and 2003. Its equalized mill rate dropped 2.2%, and yet it was able to boost total local spending by 18.0%. What magic did it use to pull this off? Between 1999 and 2002, New Canaan's total equalized net grand list (ENGL) rose 36.1%, thanks mostly to Fairfield County's robust housing market, which gave the town a larger base to tax.

Another, more surprising, source of effective property tax relief was total state aid, which in New Canaan rose 58% between 2000 and 2003. Granted, state aid is a relatively small portion of total revenues for wealthy towns like New Canaan, but it's still notable that all five richest towns had double-digit increases in total state aid, ranging from 28.1% to 94.1%, while none of the five poorest towns got more than a single-digit increase. These changes increased the state aid share of total revenues (not shown in the table) in all five of the richest towns, and reduced the share in four of the five poorest towns.

Data for the other four richest towns in Connecticut show similar trends: relatively small increases in the property tax share of total revenues (apart from the 11.9% increase in Greenwich), and sizeable increases in total local spending due to healthy percentage increases in property values (ENGL) and state aid.

At the other end of the income spectrum, the data tell a different story.

Each of the five poorest towns—Waterbury, Windham, New Haven, Bridgeport and, lowest on the per capita income list, Hartford—increased its reliance on property taxes between 2000 and 2003. Increases in the property tax share of total revenues ranged from a low of 3.4% for New Haven to a high of 13.0% for Windham, closely followed by Waterbury's 12.4%. Among the five poorest towns, Waterbury may have felt the biggest squeeze. In addition to the second largest increase in property tax reliance, it had the smallest increase in ENGL (7.4%) and the largest reduction (-11.2%) in state aid as a share of total revenues (not shown). It boosted its total local spending by a larger percentage (17.6%) than any of the other poor towns, but only by significantly raising its equalized mill rate (38.3%). Much of this fiscal pain stemmed from Waterbury's long-overdue property revaluation in 2002.

The centerfold map (pages 12-13) provides further evidence that higher income towns have generally experienced only modest increases in their reliance on property taxes, while poorer towns, especially in eastern Connecticut, generally have faced larger percentage increases in property taxes as a share of total revenues.

SUMMING UP

The bar graph on page 17 highlights some of the differences between the five richest and the five poorest towns. The growth in the local property tax base (ENGL) averaged 48.1% for the five richest towns, compared with 31.1% for the five poorest towns. This made it easier for the higher-income towns to finance local spending, as seen in their average reduction of 9.0% in the equalized mill rate, compared with an average increase of 7.9% in the five poorest towns. The poorest towns received a 6.4% average increase in state aid payments, but the average increase for the wealthiest towns was considerably larger, 59.1%. And even

(continued on page 17)

UNEVEN EFFECTS OF THE RECENT "FISCAL SQUEEZE"

	per capita income in 1999	% chg. in property tax share of revenues ('00-'03)	% chg. in equalized mill rate ('01-'03)	% chg. in local spending ('00-'03)	% chg. in equalized net grand list ('99-'02)	% chg. in total state aid ('00-'03)
RICHEST:						
New Canaan	82049	-1.9%	-2.2%	18.0%	36.1%	58.0%
Darien	77519	2.8%	-16.6%	13.9%	54.7%	28.4%
Weston	74817	3.6%	-10.5%	12.0%	40.5%	86.8%
Greenwich	74346	11.9%	-5.2%	9.0%	58.1%	28.1%
Westport	73664	0.6%	-10.7%	16.6%	51.1%	94.1%
5-town avg.	76479	3.4%	-9.0%	13.9%	48.1%	59.1%
POOREST:						
Waterbury	17701	12.4%	38.3%	17.6%	7.4%	8.6%
Windham	16978	13.0%	-6.2%	5.9%	37.1%	2.0%
New Haven	16393	3.4%	-15.9%	3.6%	56.8%	7.3%
Bridgeport	16306	8.4%	13.7%	5.8%	26.4%	7.2%
Hartford	13428	5.5%	9.7%	2.8%	27.8%	6.9%
5-town avg.	16161	8.5%	7.9%	6.0%	31.1%	6.4%

Source: Connecticut Municipal Budgets, compiled by the Connecticut Policy and Economic Council, various years.

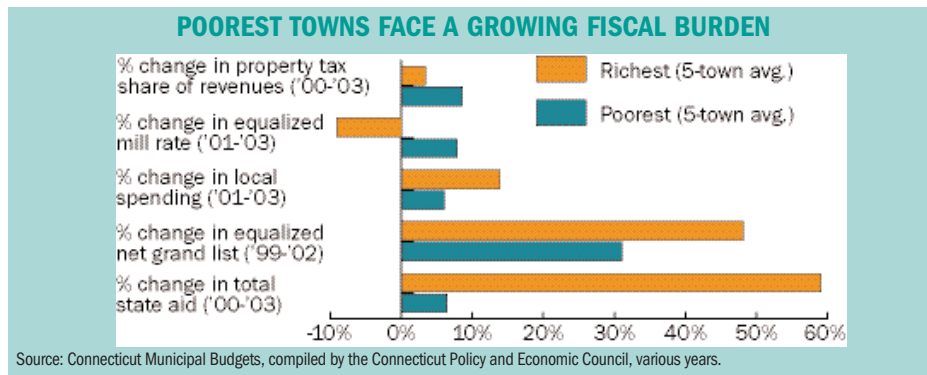
LOCAL BUDGETS (continued from page 8)

though state aid still accounts for a much larger percentage of total revenues in poorer towns than in richer ones, the state aid share of total revenues *increased* by an average of 32.8% in the five richest towns, compared to an average *reduction* of 2.6% in the five poorest towns.

Regressivity of the property tax is an old issue among public finance economists. Theoretical arguments and empirical studies of the matter are mixed. But whether low-income or high-income households bear a disproportionate burden of the tax, Connecticut town-level data seem to

confirm that pressures generated by the last recession and the fiscal plight of federal and state governments have probably made local property taxes more regressive than before. This,

coupled with an erosion of progressivity in the federal income tax, adds a few more potholes to the fiscal road ahead for lower-income households.



KEEPING (continued from page 11)

One possibility is that observed corruption may be sensitive to our choice of corruption measures. An increased rate of prosecutions of elected officials, for example, could actually reflect more the resources committed to investigating and prosecuting crime than a greater predisposition toward dishonesty among the state's politicians. Indeed, the Connecticut division of the FBI earns high marks for the efficacy of its public corruption program ("Enough Scandal to Go Around," *The Hartford Courant*, March 20, 2005). Yet in my tests of the many possible influences on our measure of corruption, variables designed to capture prosecutorial effort, such as employment and expenditures committed to criminal justice, did not provide any statistically mean-

ingful reasons for the variation in corruption across states.

Another possibility is that corruption may not be rising, but our sensitivity to political graft may be. No question that recent cases have involved high profile figures among Connecticut's elected officials. And some years have seen big spikes in convictions, especially 1994 and 2001. But a close reading of the data reveals no discernible trend over time (chart).

So whence the sense of a rising tide of corruption in the Nutmeg State? When political corruption is headline news, it may be easy to focus on the shrill news stories about guilty verdicts or pleas, instead of looking hard at the facts.

inversely with the economy, so a continuing recovery should take a further bite out of crime. But there is more we could do to raise voter turnout.

The state with the highest voter turnout (Maine) draws voters to the polls at a rate that exceeds Connecticut's by nearly 10 points. In other words, the Nutmeg State looks relatively good on this dimension, because so many other states look so bad. We could consider a myriad of possibilities, including (1) allowing e-voting, just as we now permit the e-filing of tax returns; (2) following the lead of 23 other states that have more than one "election day"; (3) permitting Election Day voter registration (EDR) rather than requiring residents to register ahead of time (now at least 14 days before an election in Connecticut); and (4) adopting more flexible voting procedures, such as mail-in ballots or no-cause absentee voting.

SHOULD CONNECTICUT DO ANYTHING (MORE) ABOUT CORRUPTION?

Whether or not corruption is on the rise in Connecticut, it clearly makes good sense, for economic as well as political reasons, to foster an environment of honest government. But how best to do this?

Connecticut's campaign finance disclosure laws are already "perfect"—at any rate, we don't know from my model whether they could be any better. And the crime rate tends to track

The evidence from my testing suggests that neither tighter restrictions on gifts, trips and honoraria, nor public financing of campaigns is likely to have much impact on corruption. But one or more fairly simple modifications to our election system to improve voter turnout could pay some significant dividends.

