

**Fiscal Stress after the Great Recession:  
A Study of Rural Counties in the U.S.**

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## Executive Summary

The Great Recession of 2008-2009 may have fundamentally altered state-county fiscal relations. The relationship is driven by weak revenue growth at the state and local level, coupled with political efforts to restrain fiscal behavior via tax and expenditure limits.

The recession appears to have resulted in a “reset” in the fiscal relations between states and county governments wherein many long-standing aid and revenue-sharing programs were either eliminated or curtailed. Many states now employ a much more targeted and limited approach to their local financial assistance. The result is chronic fiscal stress for both rural and urban counties in many states.

In a survey of county government representatives across the nation, it was reported that during the recession, many states sharply curtailed local government aid and shared revenue in response to lower state tax collections, essentially shifting service responsibilities to the local level. With the subsequent sluggish economic recovery that has not generated growth in state tax collections<sup>1</sup>, many states have exacerbated county fiscal stress by failing to restore financial aids to pre-recession levels, maintaining local service responsibilities at the county level without accompanying fiscal support, and adding to the roster of county government fiscal revenue/expenditure constraints.

The main objective of this study was to improve understanding of how rural counties across the nation are dealing with fiscal stress. Further, the study delved into state and local government relationship dynamics over the past several years and examined how that contributes to or alleviates some of the financial challenges experienced by counties in general and by rural counties in particular. A two-part survey, both online and by telephone, was conducted targeting the executive directors of state county associations. Acknowledging their fundamental advocacy role, the executive directors are uniquely situated to possess a broad understanding of member-county challenges. With a response rate of 54 percent, combining both parts of the survey, the sample was representative of all regions. Approximately 62 percent of all counties in the nation are represented in the findings.

Based on the online survey findings, the overall economic recovery in rural counties across the nation appears to be slow. Most of the respondent’s point to continued difficulty managing budgets in the post-recession period. The broad findings suggest varying degrees of economic recovery in different parts of the nation. Areas that have had faster economic recovery have been better able to move forward in dealing with fiscal challenges and those areas with slow recovery continue to experience fiscal challenges. Overall, six years after the recession officially ended, its effects are still being felt in many rural counties, further exacerbated by tax and expenditure limitations imposed by respective states.

The interviews reveal myriad issues considered critical and affecting local fiscal conditions, many of which cut across state boundaries. Similarly, every state had unique issues that influenced the fiscal standing of rural counties.

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<sup>1</sup> [http://www.rockinst.org/pdf/government\\_finance/state\\_revenue\\_report/2017-06-13-srr\\_107.pdf](http://www.rockinst.org/pdf/government_finance/state_revenue_report/2017-06-13-srr_107.pdf)

### *Rural County Challenges*

The greatest overall need that exists in rural areas is the lack of economic opportunity leading to population loss and a declining local tax base to support local public finances.

In several states, executive directors reported population migration that has created problems. Associated with the population loss and aging of the population base is a growing leadership crisis where replacements for the leadership and volunteers needed to keep rural communities vital and functioning is minimal. A small population that does not possess a wide range of skills makes economic growth difficult.

On the other hand, rapid in-migration to amenity-rich areas was overwhelming the inadequate or nonexistent infrastructure and public services. Several executive directors cited the environmental consequences of population growth.

There are growing needs related to infrastructure. Out-migration from some rural areas has left aging infrastructure and an insufficient population and tax base to support the infrastructure. This includes roads and bridges, water and wastewater, and schools. There are insufficient local resources to deal with the scale of the needs, state aid is deficient, and there is not sufficient authority and flexibility to respond independently.

Several trends are occurring that are creating greater levels of local need. Several executive directors cited their states' choices to forego expanding Medicaid funding leading to growing local health and human service's needs. The need for health and mental health services was growing faster than state and federal assistance. Many rural hospitals are no longer financially viable without public subsidy. Similarly, mental health reform keeps individuals in their communities rather than state facilities. In these instances, greater need for services is arising at the local level, and the states are helping too little or not at all.

Finally, two service areas frequently identified as challenging for rural areas were education and policing. Maintaining the local school system has challenged many rural communities and in some states, the county funds schools. Buildings, equipment, and technology were antiquated and there was insufficient local capacity to upgrade or improve. Law enforcement needs were also extensive. Movement toward community-based service and treatment was cited in relation to prison-sentencing reform that will keep more offenders in the community. In addition the opioid crisis challenges both law enforcement and the local health system.

### *State Policy Challenges*

There seems often to be a fundamental disconnect between state legislators and local officials. From the county perspective, state legislators often do not understand the needs that exist at the local level and do not trust county officials to behave in fiscally responsible ways.

States impose various forms of tax and expenditure limitations that constrain local choices and options. While these controls take many forms, they are almost uniformly viewed as impinging on local control and constraining local autonomy and choice. For their part, county officials are aware of anti-tax sentiments, but are willing to explain to their voters the needs that exist and do

what they feel may be necessary. Mostly, they want greater flexibility and choice because they recognize the diversity among counties in each state.

County officials generally seek a greater level of autonomy in managing local affairs. They often chafe at what they perceive as mandates that constrain choices or compel action. Many county officials believe the best solutions to community problems are found at the local level rather than mandated or constrained from a state capitol.

Many executive directors reported that state legislatures had issued mandates with new local service responsibilities without providing additional financial assistance. Similarly, some states withdrew assistance or service provision, effectively transferring responsibility to local government. Within the context of overarching tax and expenditure limitations, this forced reduction of other services or left other needs unmet. Executive Directors also talked about long-standing mandates, such as the requirement to fund court operations. One large case can put a substantial and unanticipated financial burden on a county. Other examples of unfunded mandates included extra pay for first responders, and requirements to participate in specific insurance and pension programs.

#### *Some Help for Rural Counties*

Largely, the executive directors felt that states have done very little in recent years to help the counties. There have been some modest enhancements of various types of revenues, e.g. gas tax, motor vehicle registration fees, or severance taxes, but nothing near meeting the needs of counties. States have done several one-time initiatives to help with road and bridge or emergency dispatch services, but have offered no enduring aid programs. Any significant local government assistance programs cited reflected actions taken many years before. For some states, state aid to counties beyond roads and bridges is limited.

A number of the executive directors interviewed reported that states replaced shared revenue aid programs with one-time funding programs. For example, states may have replaced ongoing road and bridge aid with money available by application and distributed by prioritizing greatest need or impact, revolving loan funds, or other mechanisms for infrastructure, including broadband and options for decreasing congestion in urban areas. Several executive directors cited states adding more funding for drug treatment and funding for schools for specific purposes.

A number of states have used lower oil and gas prices to increase gas taxes, and have shared some of the revenue with local governments. A handful of states implemented policies to help rural counties with transportation funding, economic development assistance, and some aid. In oil-rich states, several have expanded state funding assistance for services. This was particularly true in states where communities had experienced very rapid growth, outpacing the local capacity to meet law enforcement and social service needs.

#### *How Counties are Coping with the New Normal*

Executive directors were hard-pressed to cite examples of local government innovation. Most frequently cited was a trend toward regionalization, formal consolidation, or informal cooperation. In the realm of regionalization, several mentioned mental health and chemical dependency. Other examples included economic development, regional public health, and



regional jail facilities. In terms of consolidation/cooperation, several mentioned combined emergency dispatch services, and solid waste management. Some executive directors also mentioned counties and cities sharing costs for select services rather than duplicating them or contracting with each other for services. Some counties have reorganized and streamlined offices and services to save money. These 'innovations' offer a glimpse into what the future potentially holds for local governments, especially in rural America.

## Introduction

Local governments, both at the municipal and county level, provide vital public services affecting citizens' quality of life and creating an environment for economic opportunity. The task of maintaining and improving local public services is, however, becoming difficult and will be challenging for the foreseeable future. A confluence of factors has given rise to these challenges. First, local governments have been hard hit by the financial crisis and the Great Recession. These have hindered their ability to generate sufficient revenues to provide basic services and support economic development efforts, which are crucial to the well-being of both farm and non-farm rural families. Local governments also face increased demands based on external circumstances such as terrorism, security, natural disasters, state mandates, and citizens' increasing expectations due to rising income<sup>2</sup>. Moving forward, growth in service demands combined with demands for fiscal austerity will place local governments in difficult fiscal situations and warrant creative solutions to address the challenges.

Over the period 2009-2012, the economic environment was characterized by slow growth, high rates of unemployment, widespread government revenue shortfalls, and increasing global competition (Schizer, 2012). In addition to problems intrinsic to challenging economic conditions, since the late 1970s there have been organized political interest groups intent on constraining taxation and government initiative (*ibid.*). Today, 46 of the 50 states have some form of tax and/or expenditure limitation on local governments and more than half of the states have limited their own fiscal behavior (Amiel et al, 2009). All of this gives rise to conditions of "fiscal stress" (U.S. Congressional Budget Office (CBO); 2010, Stenberg, 2011; Scorsone and Plerhoples, 2010; Skidmore and Scorsone, 2011).

Recognition that local governments periodically experience fiscal stress is not new. Most research focuses on cities. We draw on the literature of both cities and counties and apply it to counties. Efforts have been made to measure and monitor municipal fiscal stress dating to the U.S. Advisory Commission on Intergovernmental Relations (ACIR, 1973). Since that time, there have been multiple fiscal indicator systems developed (Groves and Valente, 1994; Brown 1993, 1996; Kloha et al, 2005). Despite these efforts, relatively few units of local government systematically monitor fiscal conditions. Further, there is little empirical evidence of which indicators are most useful in prescribing an appropriate response to fiscal stress (Maher and Deller, 2007; Dougherty et al, 2000; Scorsone and Plerhoples, 2010). There is even less empirical evidence of the efficacy of any of the plethora of expenditure reduction or revenue enhancement strategies available to local governments.

In addition, there are studies that suggest the fundamental structure of the economy may have changed, and that the tax and/or expenditure system no longer fits the current economy (Jones et al, 1997; LaPlante and Honadle 2011). An example is the combination of demographic and economic changes that have transformed the retail sector. Many rural areas have lost retail

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<sup>2</sup> Public goods and services are what economists label normal goods. As incomes rise, people consume more of some types of goods (normal goods) and less of others (inferior goods). The increase may be slower or faster than the rate of increase in income. The bottom line is that as incomes increase people want more and better quality public services.

establishments due to lower family incomes, population loss, and competition from retailers in larger towns and from the Internet, leading to declining sales tax collections. In addition, retail is an inherently volatile source of tax revenue. For smaller rural counties in states where sales taxes are now an important part of county budgets this trend can make a difficult fiscal position even worse.

The primary motivation for this research was to understand the fiscal implications of economic changes for county government finances, and to identify the resulting response strategies being employed. Mohr et al (2010) along with Maher and Deller (2012) found there is a large body of research on the fiscal conditions of large cities, often drawing on international or national city/county management association surveys (e.g., Pagano et al, 2012; Maher and Sohl, 2013). They suggested several limitations of the existing research. First, the research lacks the history of the service provision, so that both new and existing modes of service provision are attributed to the circumstances that prompted the research. Second, many surveys use a yes/no response that does not allow for gradations of delivery, such as contracting for construction, but with maintenance by the local government. Further contracting with for-profit, non-profit and other governments often is not distinguished. Third, many of the surveys do not include communities of less than 10,000. Maher and Deller (2013) also found that smaller, more rural local governments are at a comparative disadvantage due to the very nature of scale restrictions and distance. Given the circumstances, understanding small rural counties therefore becomes very critical for their long-term viability and the quality of life of their citizens.

Another source of data often used by researchers is the Census of Governments, from which data on counties can be extracted. Even then, it has been observed that the quality of the data varies across states depending on whether the data are extracted from standardized reports by local governments to the state, or, in the absence of such, by questionnaires sent to local governments. The reporting and auditing requirements for local governments vary greatly across the U.S. with very weak or non-existent standards in some states (Cox and Swenson, 2006).

The alternative is to survey local governments, including small counties or municipalities, to discover how local officials assess their fiscal condition and their adaptive strategies. Girth et al. (2012) found that outsourcing by U.S. local governments was crucially affected by the local competition, or the lack of it, among contractors. Smaller local governments had fewer contracting options and often used intergovernmental contracts instead. There are also more narrowly focused surveys. For example, Afonso (2013) surveyed county governments in California and Georgia and found that they were more likely to reduce expenditures than to increase taxes in response to the recent recession. Hildreth and Miller (2002) show how the local economy affects the affordability of local public debt.

Skidmore and Scorsone (2011) examined the causes and responses to fiscal stress for cities in Michigan. They found that the fall in property values was a major contributor to stress and cities commonly responded by cutting expenditures on general government, public works, parks and recreation, and particularly capital expenditures. Two studies in Wisconsin, one on cities and villages (Maher and Deller, 2011) and the other on counties (Maher and Deller, 2013) found that “subjective” self-reported fiscal health does not correspond to the “objective” standard financial metrics. The authors suggested this apparent disconnect may be that: (1) local officials were

acting politically in stating their fiscal condition to the researchers, (2) the standard financial metrics fell short and needed to be refined, or (3) local officials were disconnected from their true fiscal condition. If the latter is true, then their strategies to address fiscal difficulties will be misplaced and the need for more focused educational programming becomes evident. The authors noted there was a need for research that delves more deeply into the basis upon which local officials develop their understanding of fiscal conditions. This research addresses several of the limitations and questions raised by the previous research and expands the existing work on small rural governments by conducting a survey that focuses on counties, especially in the rural areas across the nation.

While local governments will be dealing with fiscal challenges for the foreseeable future, our goal is not only to draw attention to these challenges but also to find areas of innovation that have helped address the challenges by sustaining and enhancing local government fiscal management capacity. Over the past 15 years, as economic hardships have occurred more frequently and with increasing severity, some local governments have responded to the 'new normal' by taking measures that are sometimes 'out of the box.' For example, Maywood, California has outsourced all of its city functions. Hall County, Georgia is considering merging city and county police departments. Deltona, Florida has outsourced public safety. Bedford County, Virginia is considering accepting private funds to build a skate park. A New York group is considering merging three counties (Stenberg, 2011). From these examples, it is evident that local governments are beginning to 'innovate' to provide uninterrupted services in the 'new normal' scenario.

## **Objectives of the Study**

The broad goal of this study is to enhance understanding of county government fiscal management and changes in state-local government relations within a context of general fiscal austerity. The study is an integrated research/extension initiative to gain a better understanding of state-local intergovernmental fiscal relations and innovative county government response strategies.

The specific objectives of the study are:

- 1) Enhance understanding of the current level of county fiscal stress;
- 2) Identify innovative local response strategies that have been implemented; and
- 3) Conduct a national comparative analysis of state policies influencing state-local intergovernmental fiscal relations.

To address the specific objectives, the study involved a two-part survey of state county association Executive Directors (EDs). Particular attention was given to collect data, both quantitative and qualitative, to assess the implications for smaller rural counties by including questions specifically about rural counties.

This study will contribute to the scholarly literature and extension educational programming. This whitepaper reports the current state of county government fiscal condition and includes a brief description of strategies to address some of the issues for use by local elected and appointed officials, extension educators, and other stakeholder groups. This whitepaper also provides a compendium of state policies influencing local government public finances and an assessment of policies that seem to help or hurt local government fiscal wellbeing.

## Methodology

The study relied on a two-part survey to generate both quantitative and qualitative data. The first part of the survey was an online survey that was conducted between January and April, 2016. The survey was targeted at 48 Executive Directors (EDs) of the State Counties' Associations. The survey was emailed to them in January, 2016 and remained active online until the end of April. Repeated reminders, both, via email and by post were sent to the executive directors encouraging them to complete the survey. While the online survey was accessed thirty-three times, some respondents completed only portions of the survey while some responded twice. For those that responded twice, the later of the attempts was included in the final data set. Overall, eighteen EDs completed the survey.

Following administration of the online survey, invitations were sent to the EDs to participate in telephone interviews. Interviews were conducted between approximately February and June, 2016. Multiple attempts were made to secure cooperation. In total, 16 interviews were conducted, about a 33% response rate. Responses were likely suppressed due to ongoing state legislative activity. In most cases, the respondent was the executive director, but in a few cases, discussion was turned over to an association research director or legislative liaison. Responses were received from ED in of all U.S. Census Bureau Regions and Divisions of the United States.

Researchers asked each respondent five standard questions (see Appendix). Follow up questions were asked to enhance understanding of the circumstance and to ensure accuracy. Interviews ranged from about 20 minutes to well over an hour.

The counties' associations are fundamentally advocacy organizations, representing members' interests before the state legislatures. It should not be surprising, therefore, that the EDs of these associations expressed a sometimes-critical view of state/local fiscal relations. In exploring the topic of state-county fiscal relations, we are able to present only one side of the story. While association EDs can reasonably be assumed to know their members collective perceptions, there is no corresponding state legislative entity to represent the state-local fiscal perspective in reverse. Thus, the story of this research is one-sided. Never the less, we believe it is an important story to tell, and would hope it facilitates discussion that can lead to a more productive and amicable relationship between counties and state legislatures

For the two-part survey, the study used a standard interview format with:

- Online survey:
  - questions related to the relative level of fiscal stress among rural counties;
- A telephone survey with open-ended questions about
  - state policies and state/local fiscal relations that help or hurt county fiscal conditions (these questions were not specific to rural counties);
  - the top issues facing rural counties; and
  - innovative responses strategies employed by rural counties.

See the appendix for the content of both parts of the survey.

## Findings

This section presents findings of the two parts of the survey that were separately conducted. Table 1 illustrates the representation of the responding EDs in the four Census Regions within U.S. and the rural-urban characteristics of the states represented.

	West	Midwest	South	Northeast
Number of respondents (online)	7	5	4	2
Number of respondents (interviews)	4	6	7	3
Number of respondents - overall	7	9	7	4
Median percent population in rural areas of responding states (2010)	19	27.6	29.4	30.5
Median percentage change in rural population of responding states (2000-2010)	-2.92%	-3.40%	-4.66%	-1.07%

Table 1. Basic information related to the states represented in the survey.

As illustrated in Table 1, EDs from 18 states participated in the online survey, a 36 percent participation rate. Seven EDs were from the Western Census Region, five EDs were from the Midwest, four EDs from the South and two EDs from the Northeast. For the direct interview portion of the survey, there were four EDs from the West, six EDs from Midwest, seven EDs from South and three EDs from the Northeast a 40 percent participation rate. Overall, EDs representing 27 states responded to at least one or both parts of the survey, a 54 percent response rate. The 27 EDs that responded represented 1,979 counties, approximately 63 percent of all counties in the nation. In addition, a comparison of the rural-urban population split among the participating state EDs indicates that the states from the Northeast with 30.5 percent had a relatively higher level of its population in rural areas, followed by the South with 29.4, Midwest with 27.6 and the West with 19 percent. The change in rural population represented by the median percentage change for the participating EDs, by region, was highest in South, where the rural population declined by 4.6 percent. In the Midwest, the decline was 3.4 percent, in West, it was 2.92 percent, and the lowest change was in Northeast where the rural population decline of participating states was 1.07 percent.

### Online Survey Findings

#### *Respondent Characteristics*

Based on the responses, it is evident that the respondents, the Executive Directors of each of their states' counties' associations, have served for a reasonably long period, with a median of 10 years. We assume that having served for approximately 10 years, they have a good understanding of the workings of county government, issues that are important, challenges they face and how they have responded to periods of economic hardship.

#### *Financial Needs of Rural Counties*

The Great Recession of 2007-09 was the most severe economic slowdown recorded since the Great Depression of the 1930s. The severity of the recession can be gauged from the fact that, at

its peak, the national economy was losing an average of about 500,000-600,000 jobs per month. The unemployment rate was close to nine percent. The motivation of the survey questions was to assess the severity of the impact the recession on the rural county financial situation. As illustrated in Figure 1, 14 of the 18 EDs that responded indicated that in the time following the recession, counties were significantly or somewhat less able to meet their financial needs compared to the pre-recession period. While this seems to be a bit surprising given that the survey was conducted almost six years after the recession officially ended, it is consistent with other studies that point to a slow recovery in rural areas (NACO, 2017) compared to urban centers where the economies either have recovered or surpassed pre-recession levels.

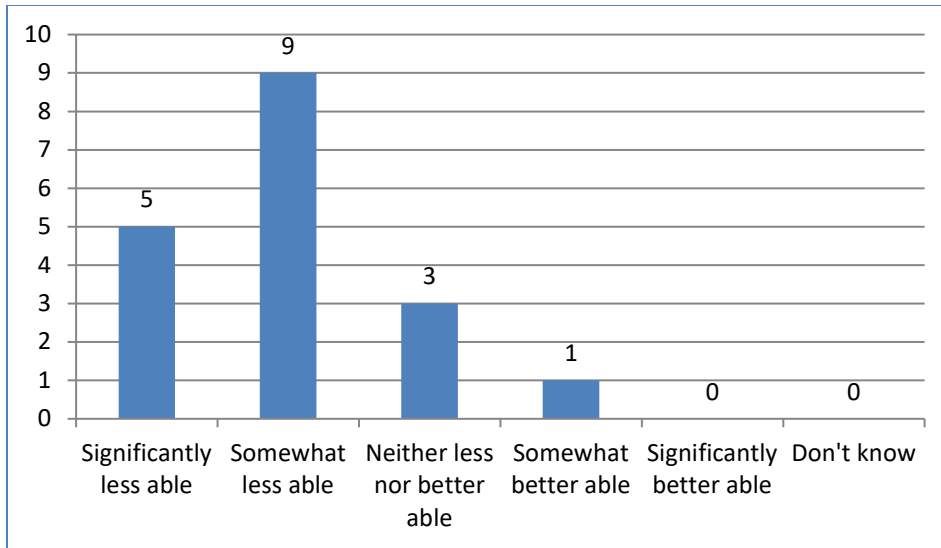


Figure 1. Financial needs of rural counties, comparing pre- and post-recession

In an effort to identify key themes from the online survey, the following section combines responses from two broad sets of survey questions, as well as two independent questions (Questions 3,4,5,6 in part 1 of the survey, see appendix). The first broad question relates to the changes that rural counties made after the recession ended in 2010, and the second question relates to the anticipated actions of rural counties in the immediate future (2017-2019). The third question relates to planning for unassigned fund balances. The fourth question relates to the liquidity of rural counties.

The responses are summarized into the following broad areas:

- Revenues
- Intergovernmental relations
- Long-term investments and debt
- Community needs
- Managing spending
- Fund balance planning and liquidity



**Revenues**

Figure 2 illustrates the responses relating to property tax revenue in the post-recession. It is well documented that local governments, especially counties, rely heavily on property tax as a source of revenue. In many states, it is the only major source of revenue for which local governments have some autonomy in setting a rate based on local needs, preferences and willingness to pay. Survey responses were mixed. The EDs in eight states witnessed increases in property tax revenue and 10 state EDs observed no change or a marginal decline following the recession. The lingering effects of the housing crisis, during which the foreclosure rates spiked, is among the factors that likely caused a decline in property tax revenue. For many communities, the economic recovery also provided a boost to their housing market with appreciation in home values that likely contributed to the increasing revenues. It is not known, however, whether the increases led to property tax revenues exceeding pre-recession levels.

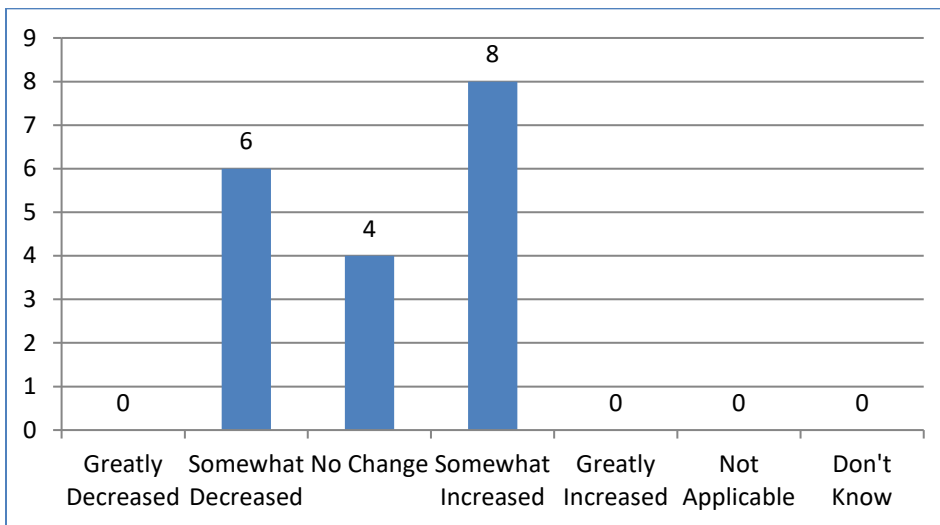


Figure 2. Property tax revenue in the post-recession

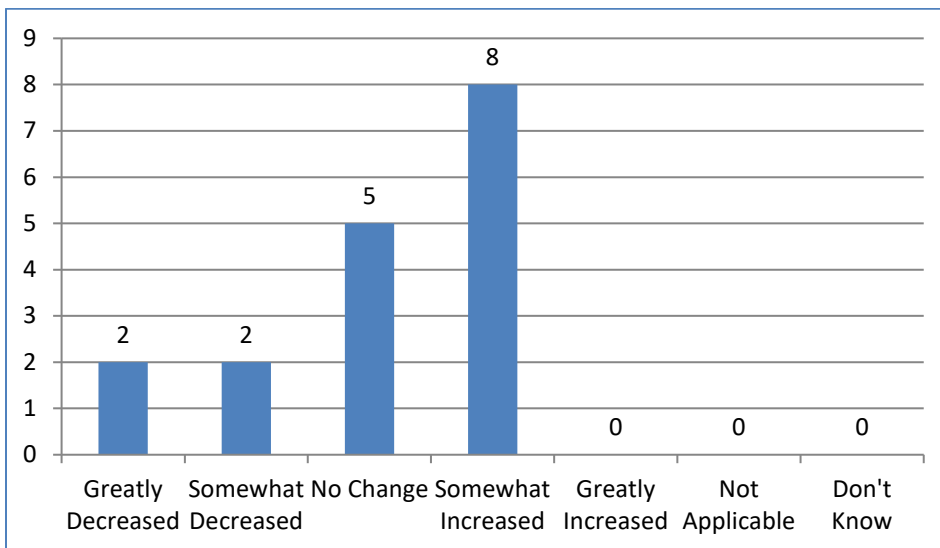


Figure 3. Fees for services, licenses, transfers, etc. in the post-recession

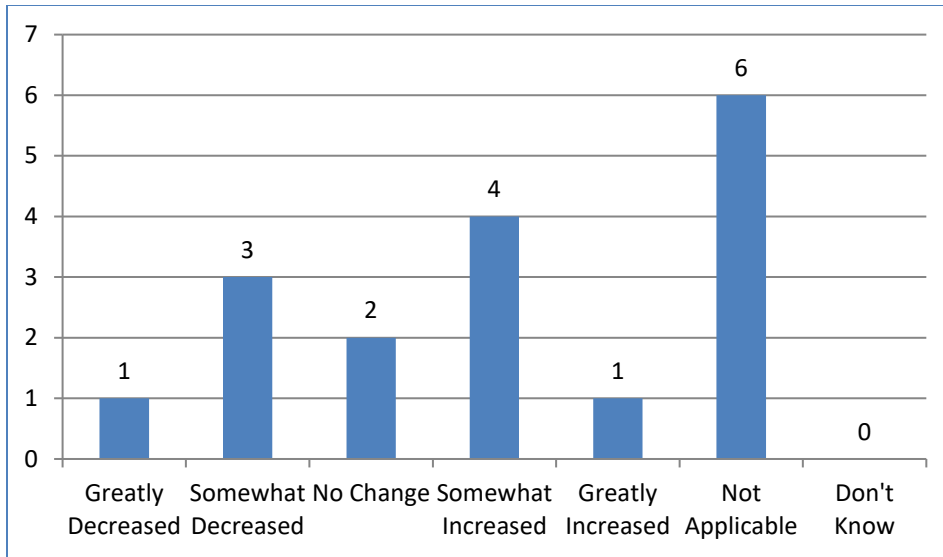


Figure 4. Sales tax revenue in the post-recession

Figures 3 and 4 illustrate responses relating to user fees and licenses and sales tax revenues for county governments. Besides property tax, local governments rely on fees and charges, and sales taxes as additional sources of revenue. However, some states do not have a sales tax, or have a sales tax only on certain purchases, with exemptions for items like food and clothing. Given the variation between states, it is not surprising that six of the 18 EDs responded ‘not applicable’ when referencing the sales tax. However, for those that did, five EDs reported having higher levels of sales tax revenue and four EDs reported a decline in sales tax revenue. This is consistent with other revenue categories and points at uneven economic recovery in rural counties across the nation. It is pertinent to add that Internet sales are increasingly affecting local government tax revenues. While a number of states have established mechanisms to track and tax transactions taking place within their jurisdiction, many sales tax dollars continue to be lost due to the online sales. Similarly, eight EDs reported that user fees and charges increased, five others reported that it remained stable four reported a decline in user fees and charges. The increase in user fees could be due to local governments substituting fees and charges for declining property tax, sales tax and intergovernmental transfers. User fees are a revenue source local governments have some flexibility to adjust to address budgetary shortfalls. However, depending on the type of user charge, there may be restrictions in the ways the revenue can be used.

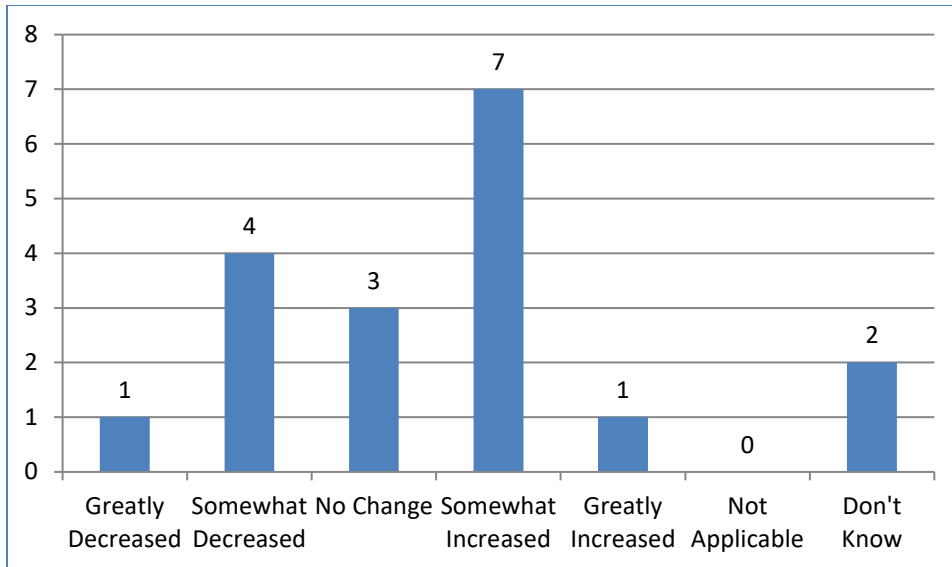


Figure 5. Tax delinquencies in the post-recession

Tax delinquencies refer to the failure of an individual or business entity to pay their taxes, usually the property tax. Following the recession, tax delinquencies were evenly divided with half of the responding EDs seeing increases and the rest witnessing a decline. This again points to the uneven economic recovery. If tax delinquencies increase significantly, it could affect a county's revenue in a significant way. A small number of tax delinquencies are inevitable because they stem from variety of reasons that might be unique to individuals and business entity. It is not surprising that half of the EDs reported increases in tax delinquencies as the impact of the housing crisis varied among states.

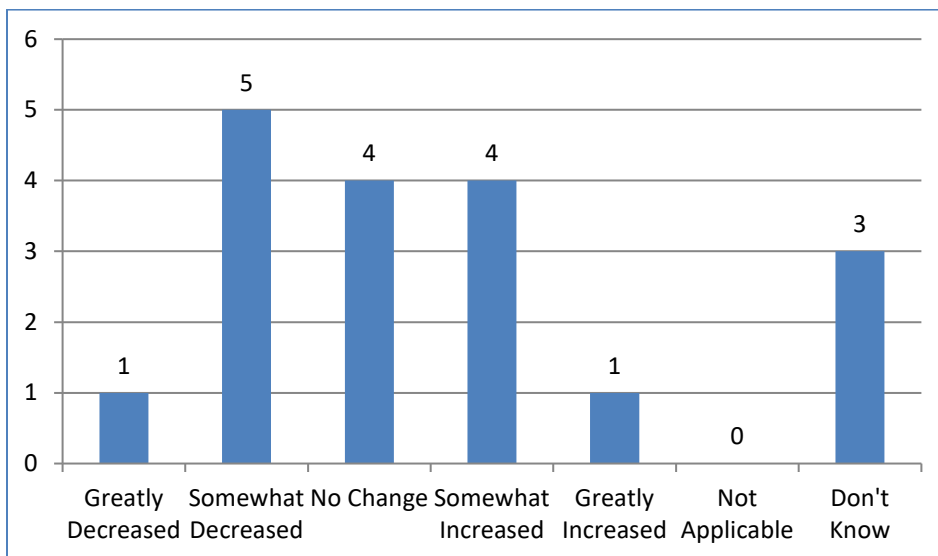


Figure 6. Home foreclosures in the post-recession

Counties rely heavily on property taxes as a source of revenue with residential properties contributing most to this source. Beginning with the financial crisis and the housing market

collapse of 2008-09, both rural and urban communities experienced shortfalls in property tax revenue. That caused a great deal of fiscal stress during the economic slowdown and the period immediately following it. As illustrated in Figure 6, in the years the economy has slowly recovered, the housing situation has improved. Ten EDs witnessed decline in home foreclosures in their respective states.

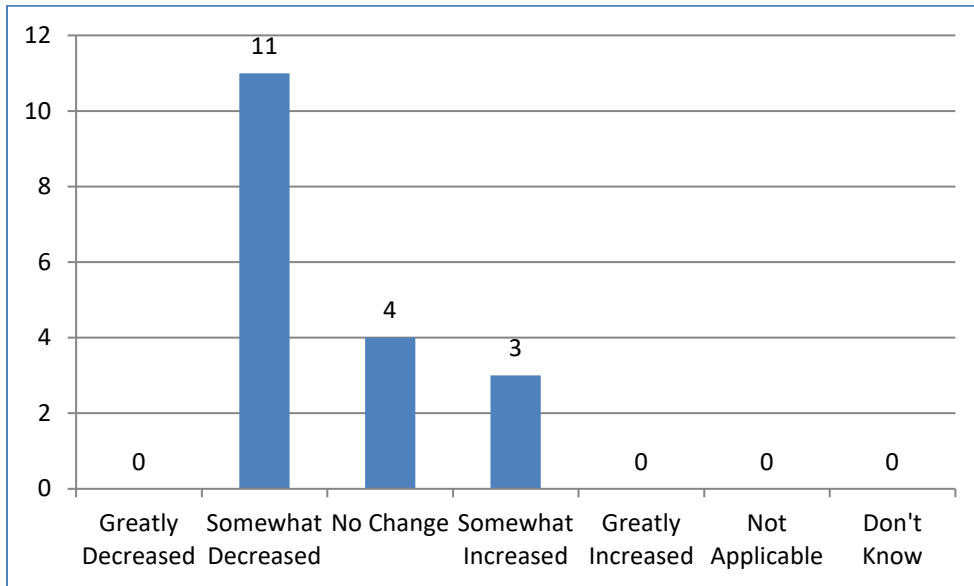


Figure 7. Population change in the post-recession

Local government finances are closely tied to demographic conditions and changes. Based on the population mix relating to age and race, household income levels, and commuting patterns of residents, demographic characteristics are shown to impact city and county tax base significantly. The focus of the study is on rural counties and the survey findings are consistent with the trends observed in many rural areas that continue to experience slow but steady population decline. With 15 EDs reporting either a decline or no change, it is apparent that the level of fiscal stress in many rural regions is being exacerbated by depopulation. It should be acknowledged, however, that there also are many rural regions across the nation that are experiencing population growth.

Figures 8-11 summarizes the responses about how rural counties might respond to a host of variables related to their revenues in the immediate future.

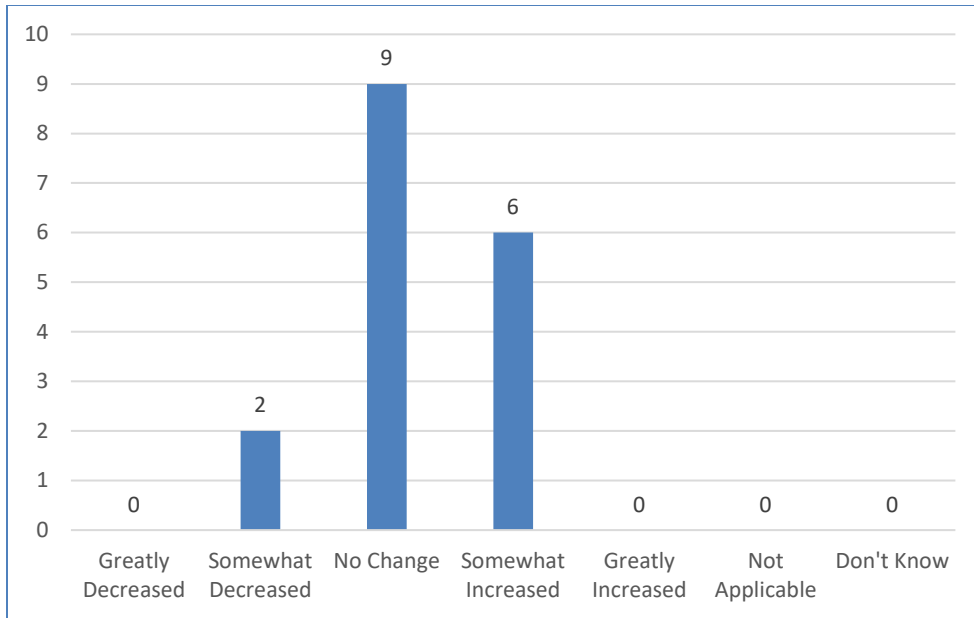


Figure 8. Anticipated property tax rates during 2017 and beyond

Property tax is the largest source of revenue for a majority of rural counties. While six EDs expected property tax rates to increase, the majority of the EDs reported that the property tax rate would remain steady. Another aspect of property tax revenue relates to the changes in methods used in valuing different property classes and the various state-mandated laws that constrain changes in valuation. One significant trend potentially affecting property tax revenues is the ‘dark store’ strategy being proposed or implemented in several states. This lowers the value of commercial property for tax calculation purposes (Farmer, 2016). With modest increases in home values, stable property tax rates will generate additional revenue. That may explain responses about no change in future property tax rates.

While the majority of EDs anticipate property tax rates will remain stable, there is a large group that expect an increase. Some increase in property taxes might be expected because many counties continue to experience lower levels of state and federal funding coupled with a general increase in state-mandated spending. Given the reliance on property tax as a source of revenue and variation in property valuation growth, increasing the tax rate seems the logical step. In addition, with economic conditions slowly improving, many county governments are undertaking capital improvements that require increases in property tax rates to pay off debt over the long-term.

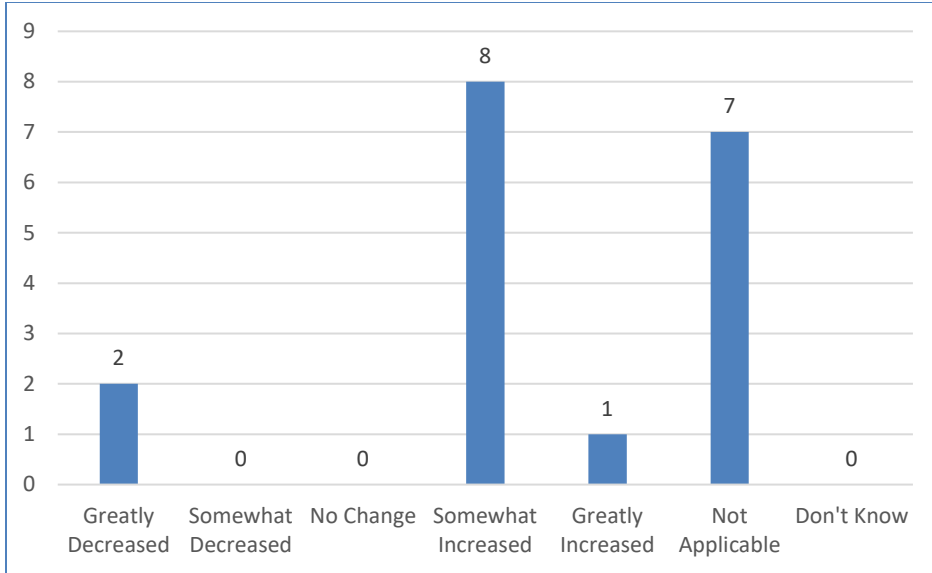


Figure 9. Anticipated sales tax rates during 2017 and beyond

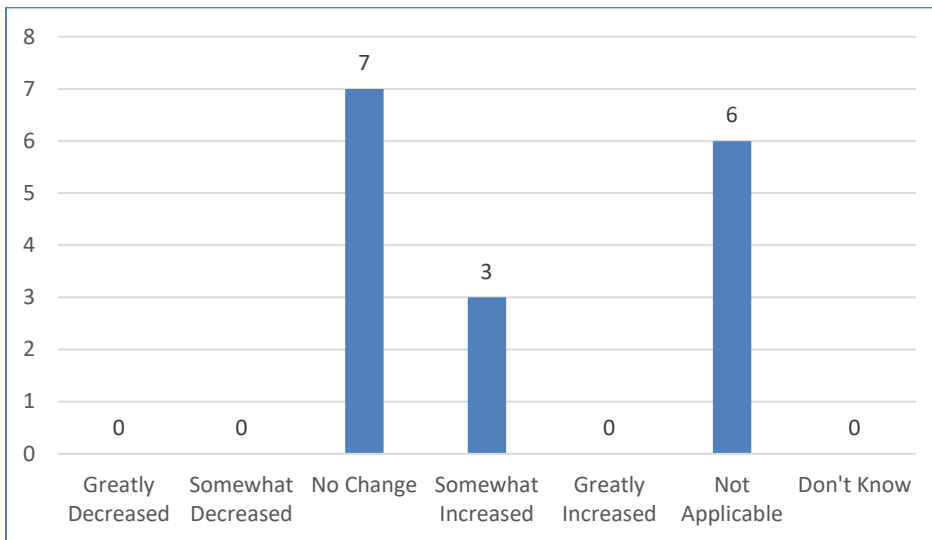


Figure 10. Anticipated new sales or use taxes during 2017 and beyond

Figures 9 and 10 illustrate the anticipated changes to sales tax rates and use taxes. A “use tax is a sales tax paid for purchases made outside one's state of residence on taxable items that will be used, stored or consumed in one's state of residence and on which no tax was collected in the state of purchase. If the purchase would have been taxed had it been made in the purchaser's state of residence, then use tax is due. The use tax rate is the same as the resident's local sales tax rate, which includes both state and local sales taxes. A resident who does not pay use tax may be subject to interest and penalties”(Fontenelli, 2017).

Just like the property tax rate, county governments expect sales and use tax rates to increase in the near future. With the limited options the county governments have to raise revenues, a

marginal increase in sales and use tax rates could generate revenues to help fill revenue a shortfall, especially at a time when consumer spending is strong.

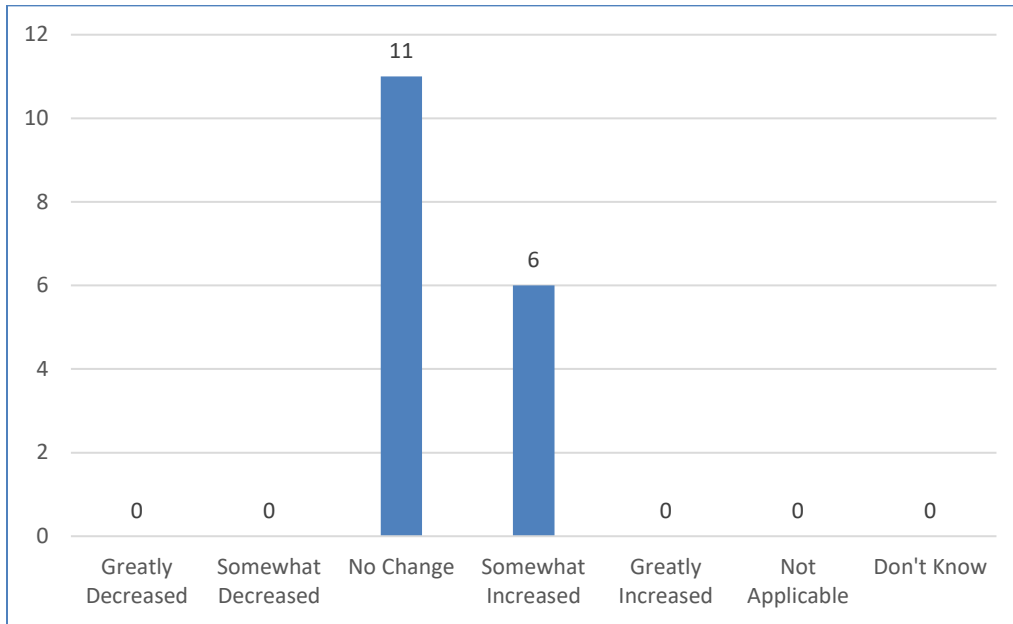


Figure 11. Anticipated charges for fees, licenses during 2017 and beyond

On the sales and other taxes, half of the EDs did not anticipate increases. A number of states do not have sales tax, which explains their responses. For those states that do have sales tax, 11 EDs indicated no change in sales tax rates. Given that sales tax is an elastic revenue, increasing and declining with periodic economic cycles, an increase in sales tax rates seems like a logical step for counties experiencing fiscal challenges. The period of recovery following a recession is expected to be one where sales tax rates as well as increased levels of consumer expenditure increase revenues for county governments.

As in the case of sales tax rates, periods of economic decline are characterized by a decline in user fees and licenses and during a phase of recovery and a robust economy, user fees and charges are expected to increase.

### ***Inter-governmental relations***

The principle of fiscal federalism allows various governmental functions to be divided among federal, state and local levels. This requires coordination and resource sharing between the different levels of government. That typically involves the transfer of funds between the federal government and states, between states and local governments, and between local governments. While some fund transfers are mandatory and are offered as aid, other transfers are in the form of competitive grants. Clearly, economic cycles have an impact on the scale of these transfers. Several funding formulae that rely on population size also affect the rural areas negatively compared to their urban counterparts since population decline in rural areas is more prevalent. In addition, legislative changes at the state level on cost sharing also affects the flow of funds and affects state-local fiscal relations.

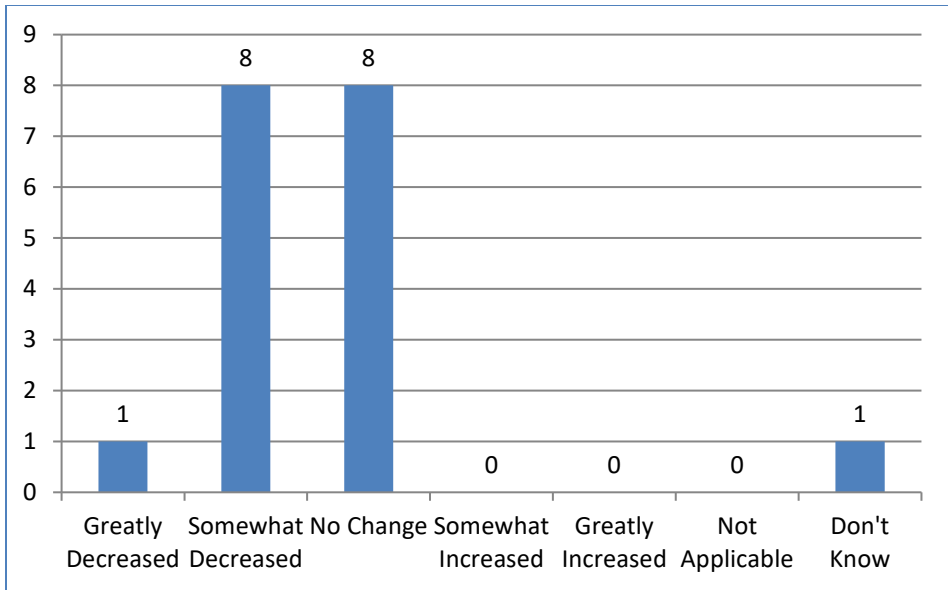


Figure 12. Federal aid in the post-recession

Federal aid (Figure 12) refers to intergovernmental money transfers in the form of grants or loans that local governments receive to make improvements to capital assets such as roads and bridges. With federal government itself dealing with a slow economic recovery, it is not surprising that not one state reported an increase in federal aid. All reported no change or a decline in intergovernmental money transfers. This is significant because needs related to infrastructure in rural communities continue to grow, and frequently require federal and/or state assistance to make these investments. These directly affect the quality of life that people experience.

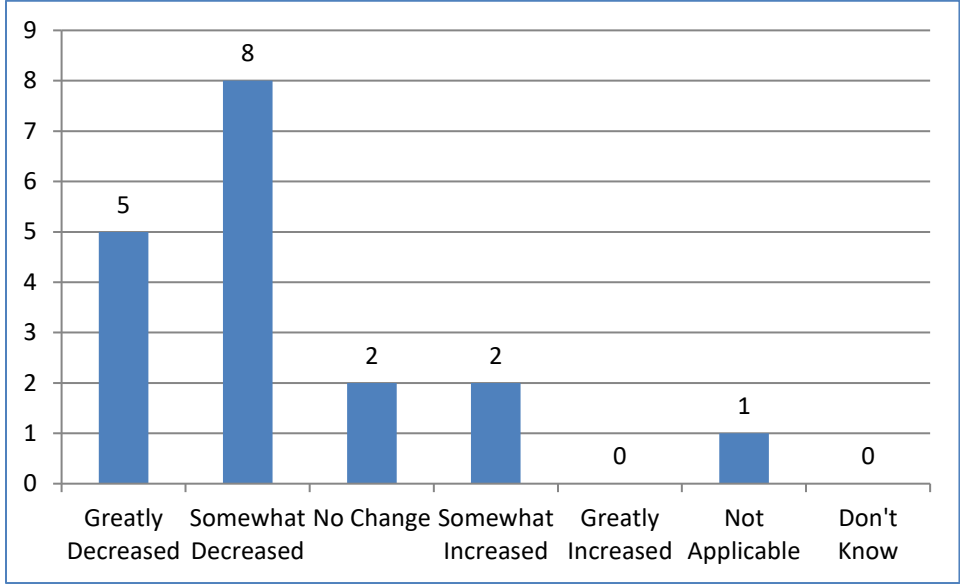


Figure 13. State aid in the post-recession

State aid refers to monies received by counties from their respective states. The majority of EDs that responded point to marginal or large declines (Figure 13). Only two EDs reported a small



increase in state aid. While there has been an improvement in the national economy, it is apparent from the survey responses that those might be concentrated in urban areas. This once again points at a slow economic recovery in many states and especially in rural areas throughout the nation. It is significant to mention that the aid received from the state governments declined by a greater degree compared to federal aid.

***Long-term investments and Debt***

Much of the growth and progress the United States achieved over the last century was made possible due to its strong and reliable public infrastructure. Commonly referred to by the general public as public goods, the private sector has no incentive to invest in them. It is usually the governments’ responsibility to make investments to maintain as well as create new public infrastructure. Public investments in assets, which includes highways, roads, bridges, public schools and higher education institutions, water and sewer systems, ports, railways, airports etc., allowed the market economy to thrive, creating wealth, opportunity, prosperity and improving quality of life of residents. It now is becoming more apparent that public infrastructure is aging and there is a growing need for major investments to rehabilitate existing infrastructure and create new assets. One of the key aspects of public infrastructure is not just the capacity it provides to local governments to facilitate the provision of essential services to residents but also the critical role it plays in assisting private farm and non-farm businesses to carry out their production and distribution activities. This translates into forward and backward economic linkages that, through a cascading effect, positively contribute to the national, state and local economies. In addition to these direct benefits, expenditures made toward periodic maintenance, rehabilitation and replacement of existing public assets help the economy by way of supporting a number of jobs.

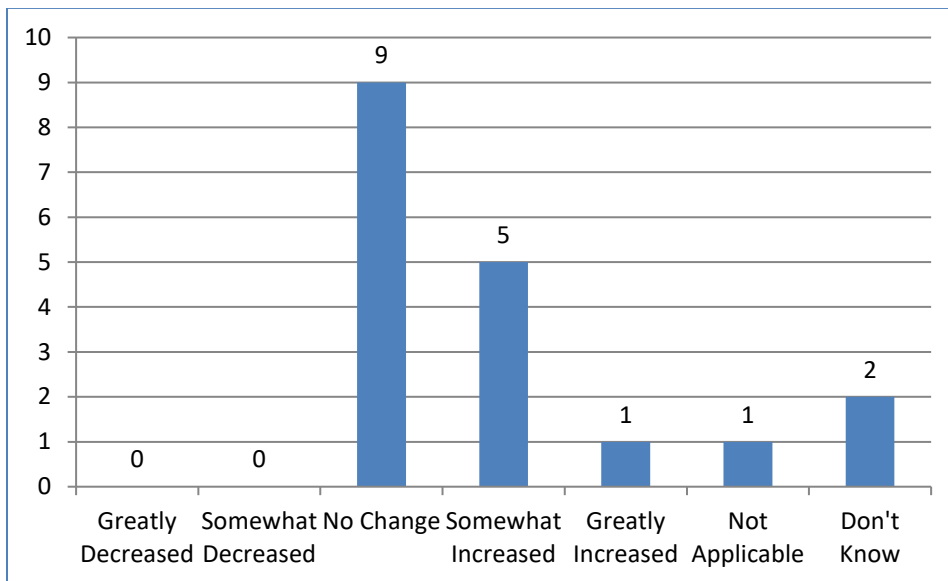


Figure 14. Debt in the post-recession

Local government debt usually refers to borrowing through municipal bonds that are repaid over a specified period with interest. Given that there is uneven economic recovery between states, it is not surprising that more than half of the EDs responded ‘no change’ in debt compared to the

pre-recession period (Figure 14). However, it is also apparent that in some parts of the country, counties are making long-term investments on community assets.

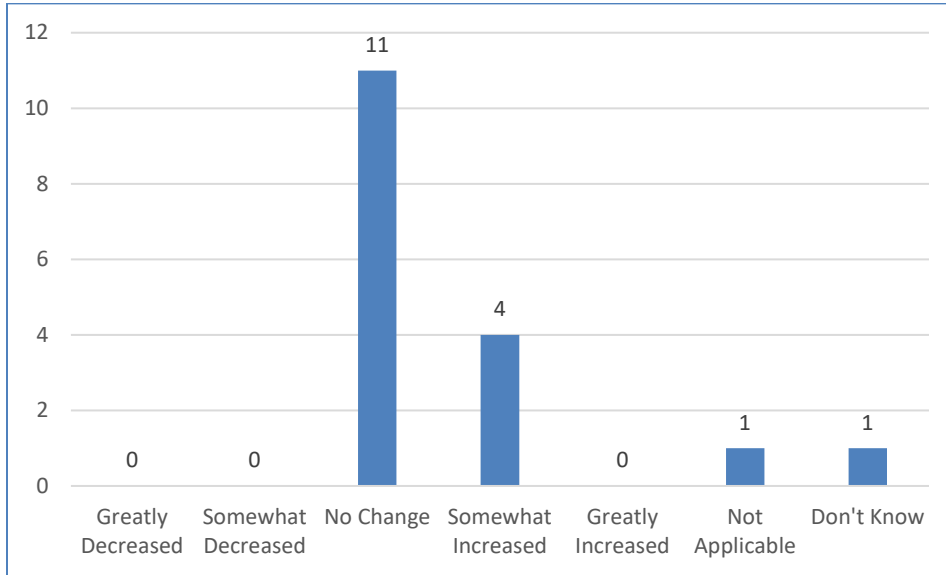


Figure 15. Anticipated amount of debt in the post-recession

With the uncertainty that prevailed in the economy after the recession officially ended, most county governments, especially those in rural areas, did not take on additional debt to fund capital projects. A small number of the responding EDs, however, point at marginal increases in borrowing (Figure 15). This trend may be due to the slow pace of economic recovery in rural parts of the nation as well as uncertainty about the future that led to most rural counties to defer any major investments.

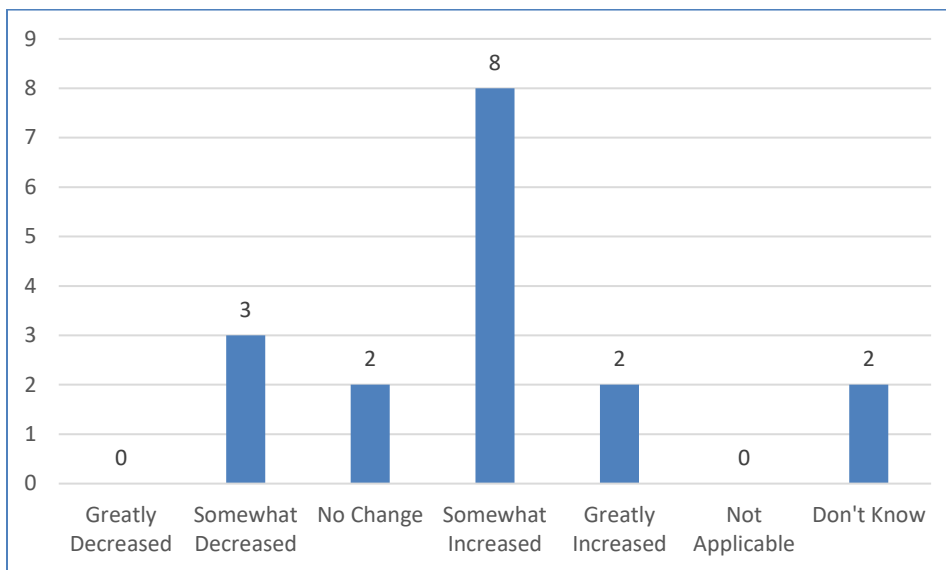


Figure 16. Anticipated actual infrastructure spending revenue in the post-recession

Driven partially by the funds made available through the American Recovery and Reinvestment Act, also referred to as the stimulus package, the federal government provided grants to state and local governments to invest in major transportation and other physical infrastructure to increase the flow of money within the economy as well as to rebuild crumbling infrastructure. Approximately \$250 billion was spent during 2009-2012. Survey respondents point at this, with a majority of EDs reporting an increase in capital spending.

Overall, based on findings of the survey, rural counties made investments in capital projects and large portions of the finding came in the form of aid rather than borrowing from the capital market.

***Community Needs***

The questions relating to perceived community needs and how they are being met are intended to help understand the gap between perceived needs in rural counties and the ability to fulfill them. The questions relating to need focus on public safety, infrastructure, human services and general government operations, all of which have a bearing on economic opportunity and the quality of life in rural communities.

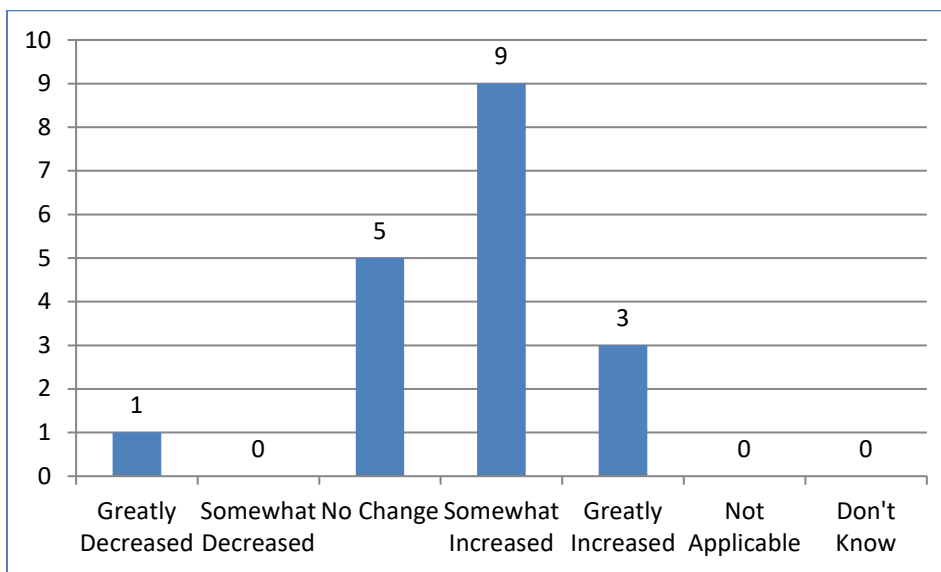


Figure 17. Public safety needs revenue in the post-recession

Broadly, public safety expenditures relate to spending on law enforcement operations, emergency management, jail, flood control, fire, animal control and other related services. While law enforcement typically accounts for most of the expenditures, other have occasional spikes due to natural disasters or major capital outlays. Twelve of the 17 EDs that responded reported either a somewhat or a great increase in public safety spending since 2010 (Figure 17). Given the varied and unique circumstances that dictate the level of spending, it is challenging to pinpoint to any specific set of factors that have contributed toward an increase in public safety spending in rural counties.

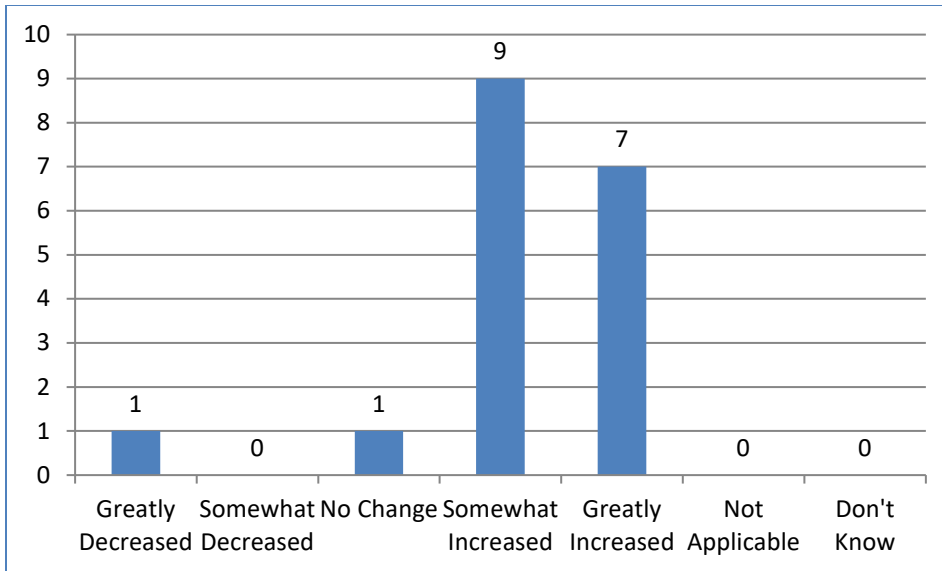


Figure 18. Infrastructure needs in the post-recession

Infrastructure refers to the built environment that includes roads, bridges, public buildings, and water and sewer systems. It is known that given the age of infrastructure in the nation, in both rural and urban communities, there is a great need for investments to upgrade, replace and create new infrastructure. As is illustrated in Table 18, with 16 EDs responding to greater infrastructure needs, this aligns with the general narrative on the need for greater public investments.

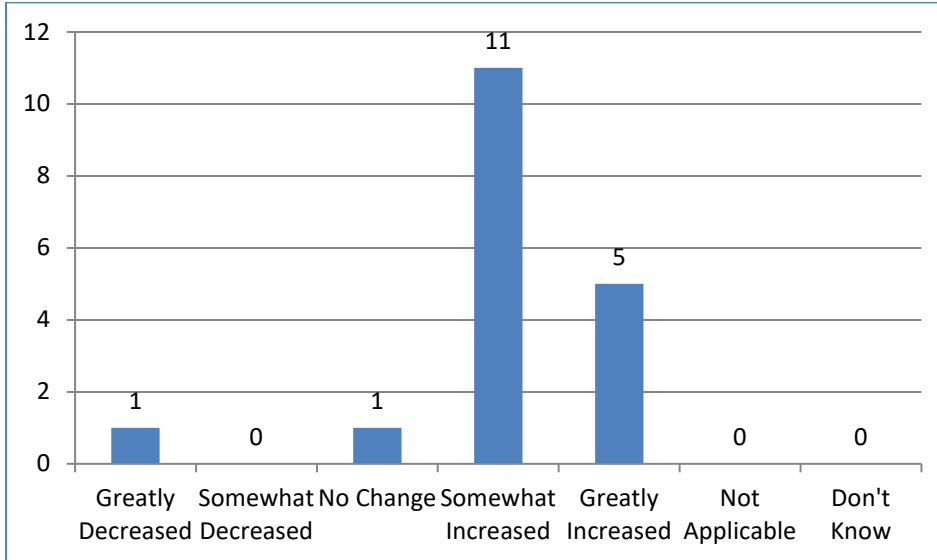


Figure 19. Human service needs in the post-recession

Overall, human services at the county level include services for aging, children and youth, substance abuse, early intervention, juvenile justice, mental health, mental retardation, nursing homes, adult services and veteran affairs. Beginning prior to the onset of the economic recession and continuing through it and the subsequent recovery, rural communities were hit hard by high unemployment rates that increased the need for human services. In addition, the period also

witnessed the drawdown of U.S. military from Iraq and Afghanistan and increased the need for different types of human services (Figure 19).

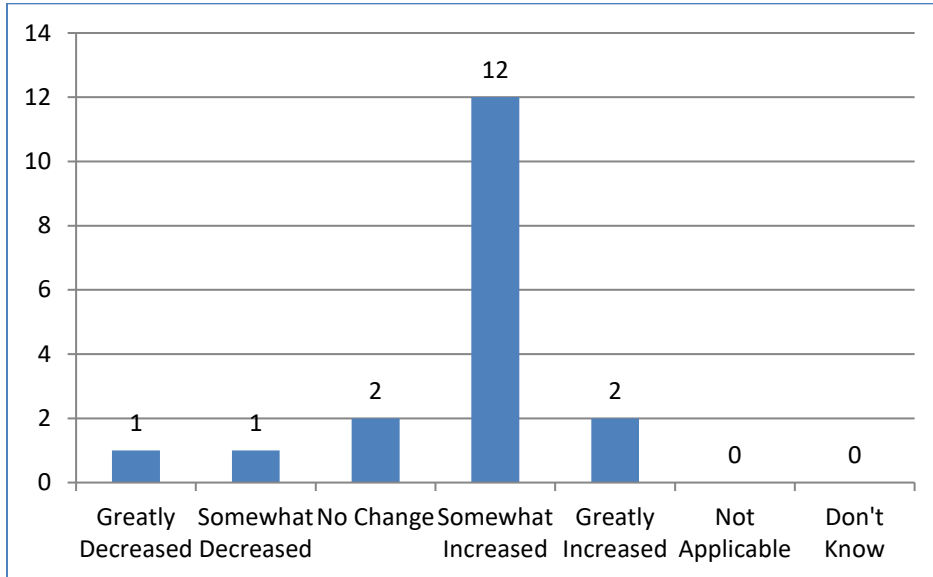


Figure 20. General government operations needs in the post-recession

General government operations refer to the day-to-day workings of county governments. As the economic recession officially ended, counties and states continue to experience a surge in demand for various types of services that residents need. As a result, majority of the EDs that responded observed a general increase for government operation needs (Figure 20). This is consistent with the general increase in demand for services anticipated in the near future (Figure 21)

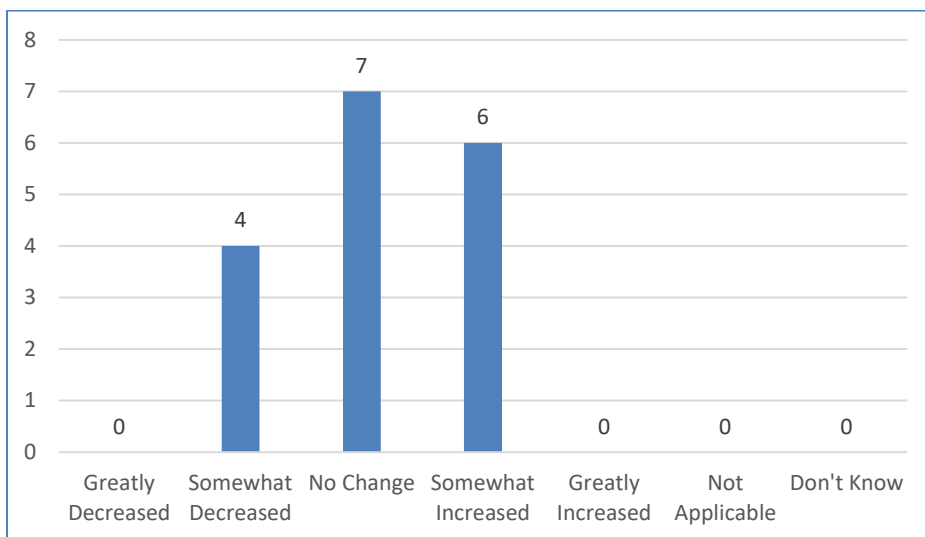


Figure 21. Anticipated amount of services provided in the post-recession

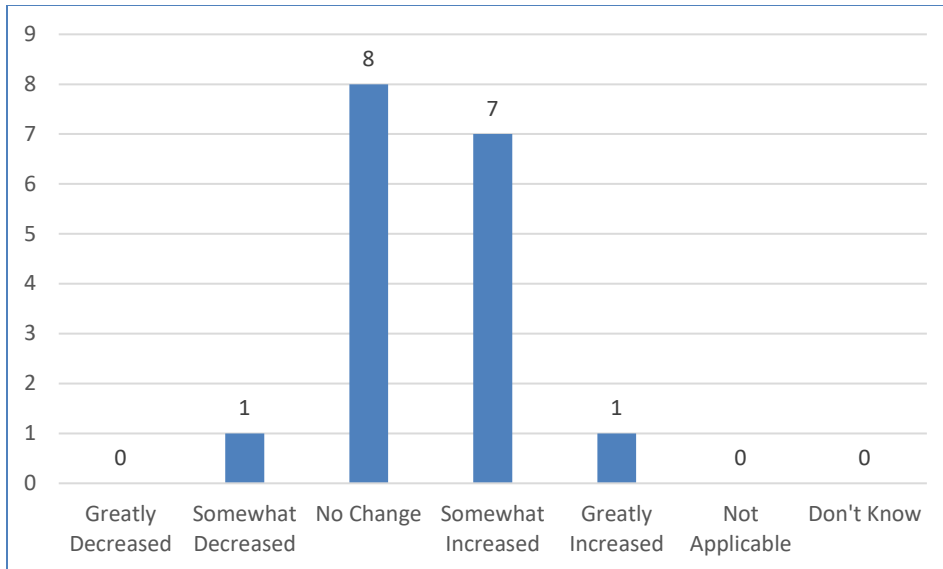


Figure 22. Anticipated actual public safety spending in the post-recession

Public safety usually refers to law enforcement, but also includes fire, animal control, emergency medical services and emergency management. While it is difficult to pinpoint exact reasons that led to increases in public safety spending, a few circumstances likely contributed (Figure 22). Law enforcement, especially in those states plagued with the surge in drug addiction, had a greater role to play. In addition, high unemployment rates in rural areas may have contributed to higher levels of crime. Of course, other local and unique factors may have also contributed as well.

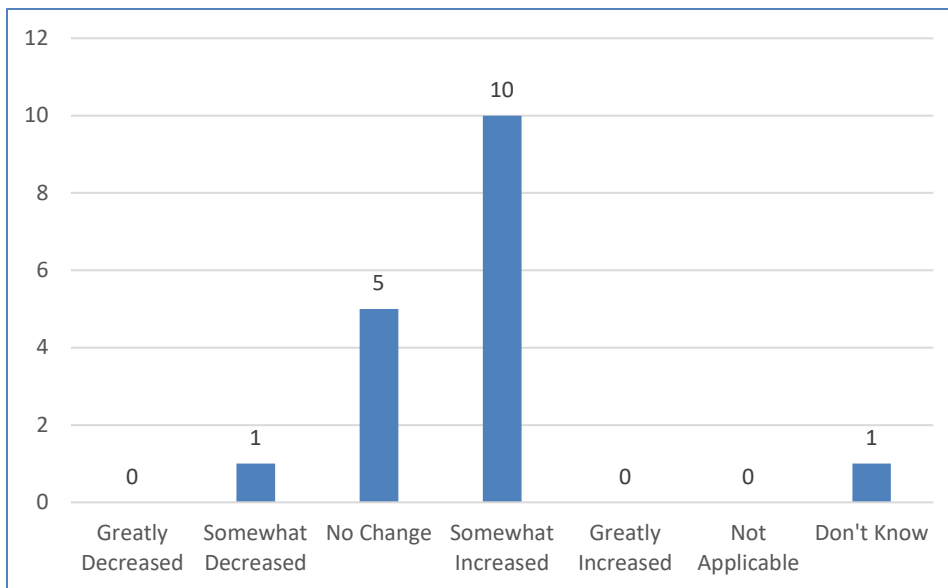


Figure 23. Anticipated actual general government operations spending in the post-recession

In ten states, EDs reported government operation spending increases (Figure 23). Five EDs reported no change and one ED reported a marginal decline. In a post-recession recovery, there

tends to be a spike in the demand for services from government (Schalitzer et al, 2012). These increased demands may appear due to several types of changes in the economy including employment, housing, healthcare and several other key sectors in a community. Given the magnitude of the last recession, it is likely more states experienced a backlog of pent-up demand for their services.

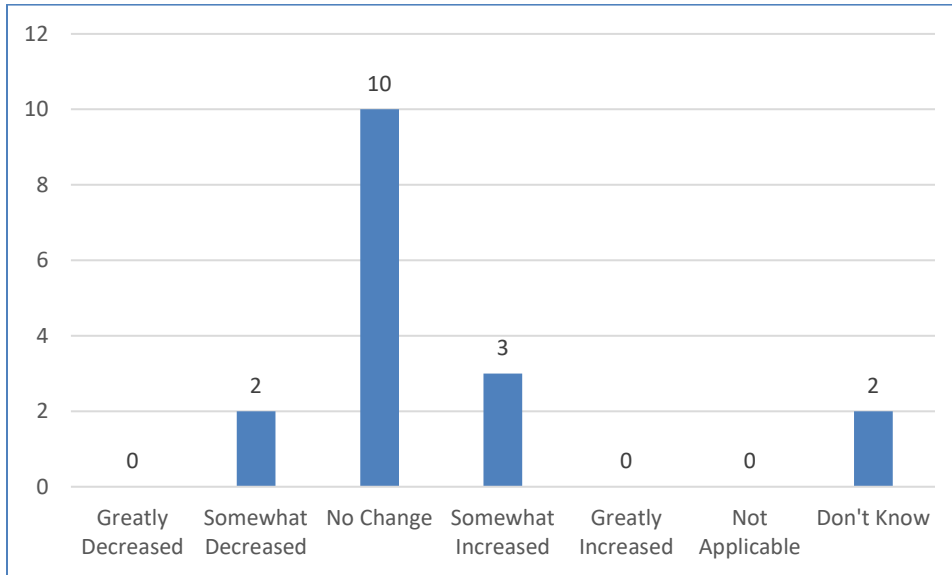


Figure 24. Anticipated economic development related spending in the post-recession

It is not surprising that economic development related expenditures either remained flat or declined in the period after the recession (Figure 24). Given the very high level of unemployment that existed in many states, especially in rural communities, there were few economic opportunities and little capacity for new investment. Three EDs, however, indicated that the level of spending in this category increased marginally.

***Managing spending***

Major concerns at every level of government include the relative level of spending, providing the best possible service at lowest possible cost, ensuring those who need services can access them, and that the appropriate mix and level of services . While all of these are subject to debate, there is consensus that managing expenditures effectively is a core goal.

One of the main aspects of the economic recovery since the recession officially ended is the decline in government jobs, especially at the local level. In the private sector, the new jobs created now exceed the total number of jobs lost because of the recession. Meanwhile, local governments have witnessed a net reduction in jobs. The survey findings are in line with this overall trend. The majority of the EDs reported either a decline or no change (Figure 25). A common practice in response to budgetary shortfalls is to freeze employee (National League of Cities, 2016). The findings of the survey point at a similar trend with 10 EDs reporting a marginal decline in county government jobs while six reported stable employment numbers. Only two EDs reported having witnessed new hiring during the post-recession phase.

Also, as time has progressed, more states have elected officials who believe in reducing government spending which also contributed to the slow growth in local government jobs, even though the population in some counties and demand for services continue to increase. In addition to reducing employment, wages may also be decreased by hiring different types of employees. The EDs report a variety of wage changes. Several report wage decreases. The majority did not observe wage changes and only 7 EDs report some wage increase in their states. This variation again suggests unevenness in the economic recovery across the country (Figure 26).

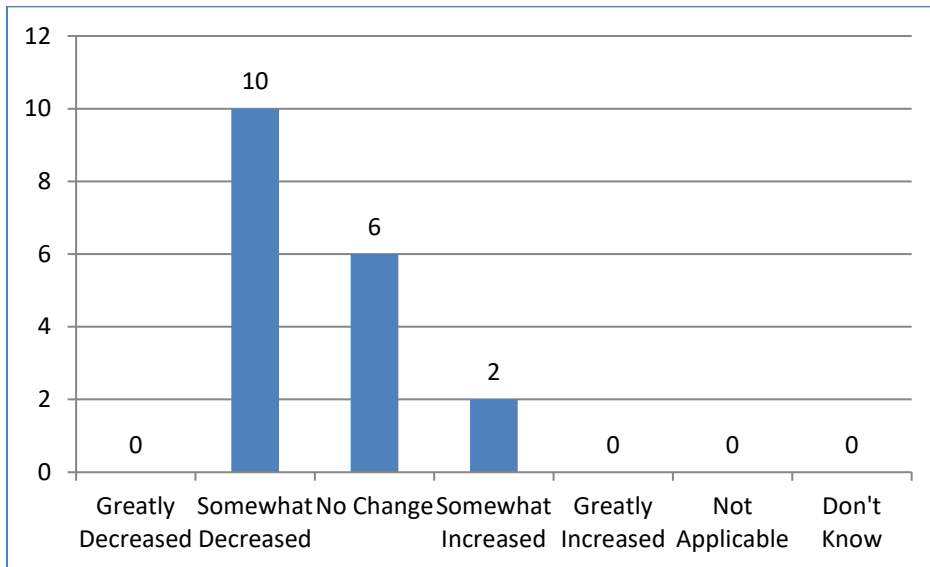


Figure 25. County government employment changes in the post-recession

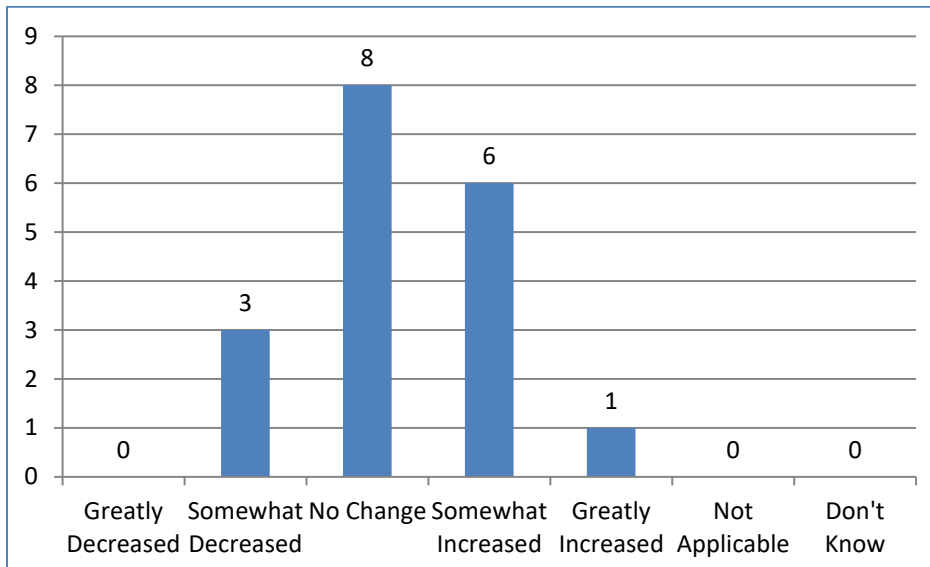


Figure 26. Wage rate changes in the post-recession phase



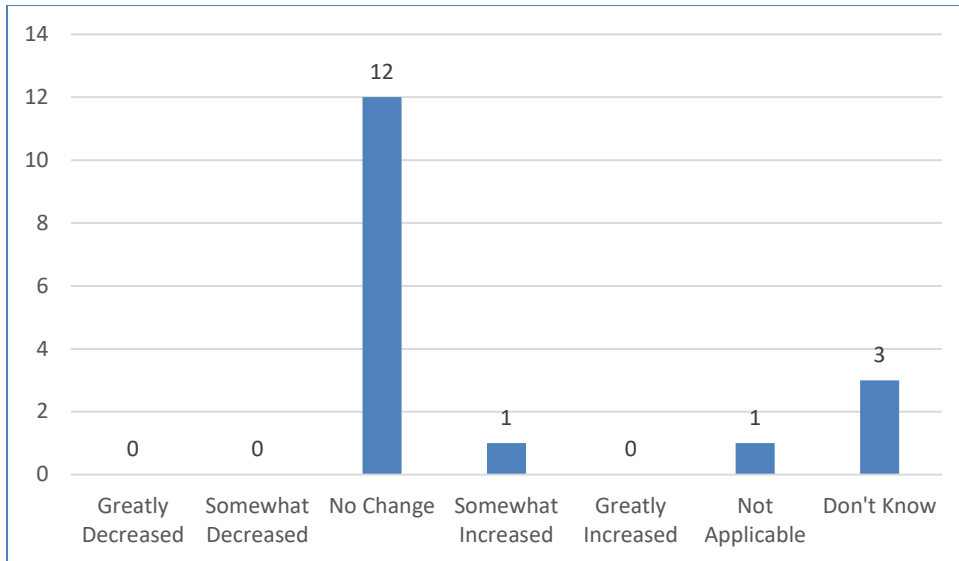


Figure 27. Anticipated level of sale of public assets in the post-recession

Public assets refer to those assets owned by federal, state or local governments. This may include buildings, land, and equipment. The assets or property that the government owns could be acquired either through normal purchase or by way of other means such as seizure due to non-payment of taxes etc. Usually, government property is exempt from taxes. In general the EDs did not expect an increase in the sale of public assets, which would be a way to increase short-run revenues (Figure 27).

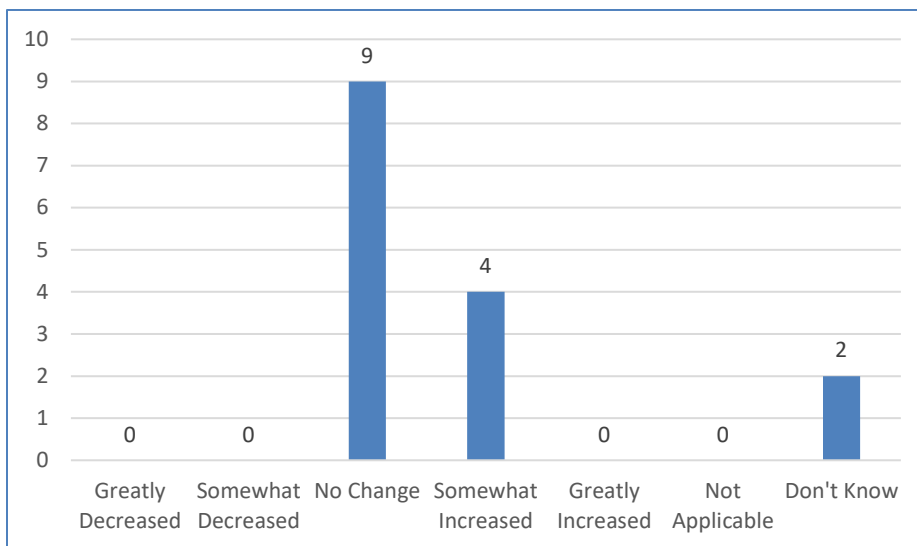


Figure 28. Anticipated level of privatizing or contracting of services in the post-recession

In an effort to make services more efficient and deal with the growing burden of revenue-expenditure mismatch, contracting of services may be an alternative. Examples include emergency services, construction projects, road and bridge maintenance, waste disposal, etc. In

some areas the EDs expected there may be a small increase in contracting (Figure 28).

Figures 29-31 illustrate the growth in cost of employing the local government workforce. This includes wages, health benefits for current employees and retired employees as well pensions for retired employees

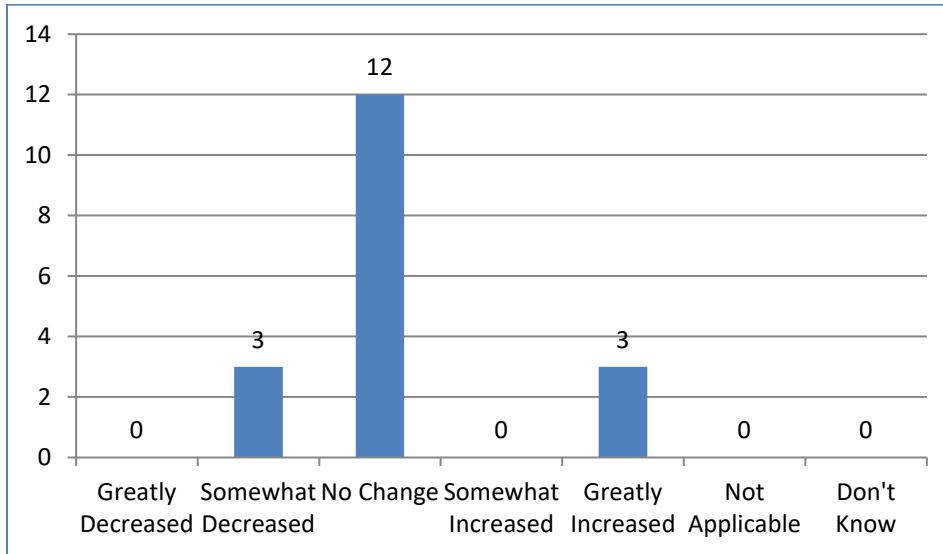


Figure 29. Funding of pensions in the post-recession

Pension obligations for retired employees have been under increasing scrutiny. Many states and municipalities have fallen short of fully funding retirement programs. As more employees retire, there is concern that maintaining a sustainable pension plan might get more challenging. Based on the findings, it is a positive sign that 15 EDs indicated there has been either no change or an increase in pension funding. Three EDs reported a decline in funding pensions and other retiree obligations (Figure 29).

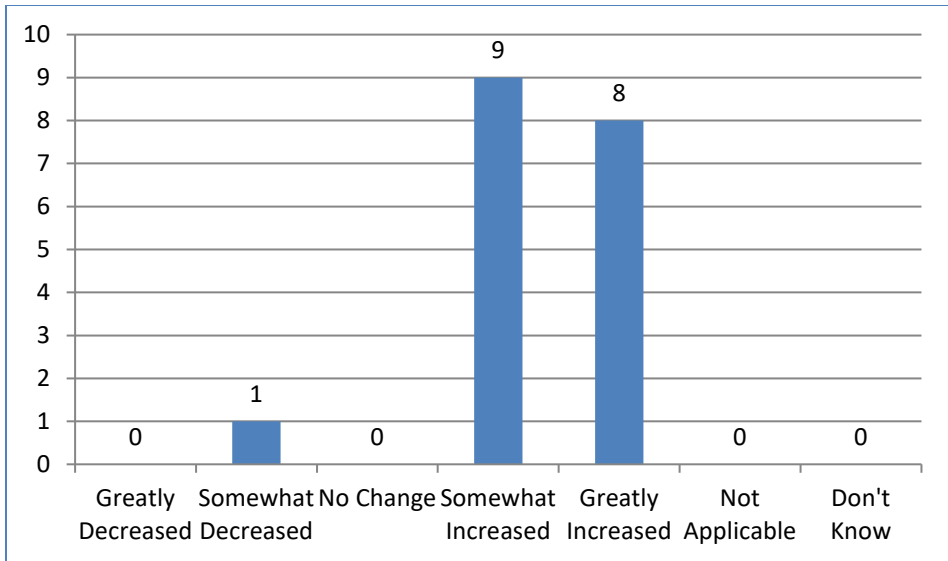


Figure 30. Employee benefit costs in the post-recession

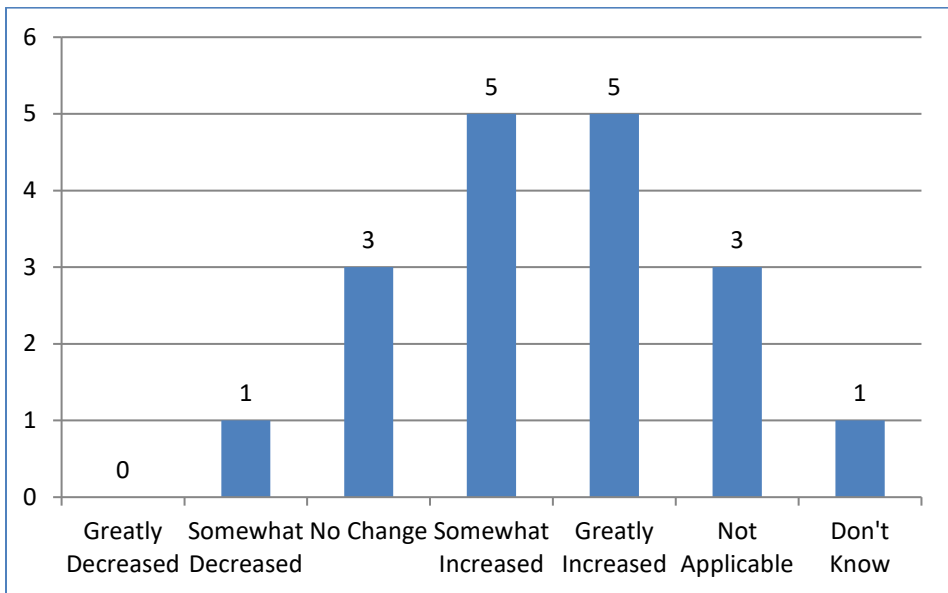


Figure 31. Retired employees' health benefits in the post-recession

Across most of the states, it is apparent that local governments have experienced a marginal to large increase in retiree health benefit costs (Figure 30). The increase is higher for current employees in comparison to the retired employees (Figure 31).

Figures 32-36 illustrate areas where county governments expect to see increases or decline in services and associated expenses. Almost half of the respondents expect the level of human services (Figure 32) to increase in the next several years. The rest half expect no change and two EDs anticipate a decline in human service spending.

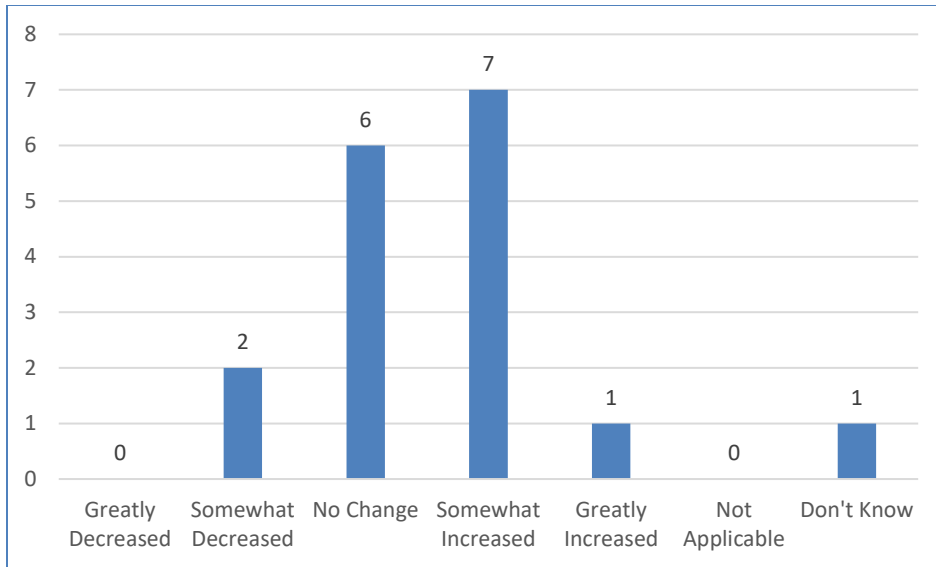


Figure 32. Anticipated actual human services spending in the post-recession

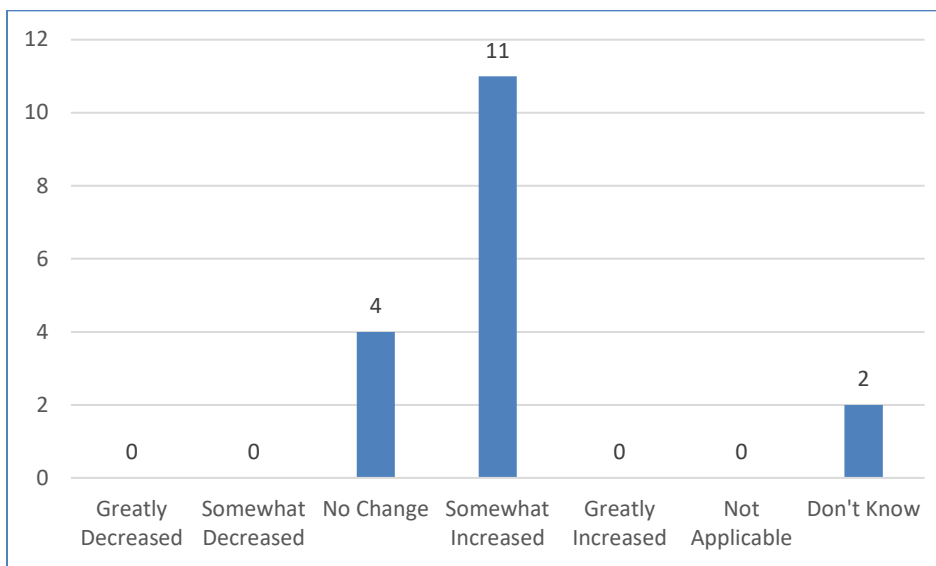


Figure 33. Anticipated inter-local cost-sharing with other governments in the post-recession

In an effort to reduce administrative costs and keep providing services, a number of local governments enter into cost-sharing arrangements with other local governments. This is especially true in the case of small and rural communities. A majority of EDs responded that they anticipate that trend to increase in the near future (Figure 33).

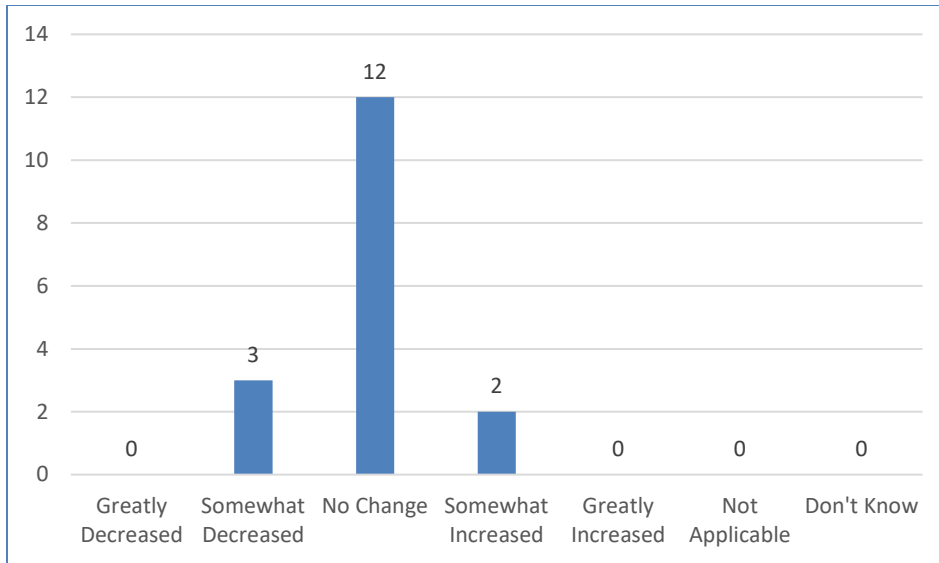


Figure 34. Anticipated workforce hiring decisions in the post-recession

Within a slow economic growth and population decline environment, most EDs anticipate no new hiring and maintaining current levels of staffing (Figure 34). This is a trend observed nationwide in earlier studies (National League of Cities, 2016). Given budgetary pressures, hiring freezes are a more acceptable and relatively milder strategy. While not keeping up with staff as demand for services grow could become problematic, it is widely accepted as an effective strategy to reduce short-term spending. On the contrary, as illustrated in Figure 35, about half of the responding EDs believe that there will be no changes in staff or a marginal increase in layoffs. In a similar vein, several EDs are expecting new hiring to fill positions if economic conditions improve and county governments have the resources available. As Figure 36 illustrates, there is a need for new staffing and given the opportunity, counties would rather hire. However, more than half of the EDs responded that there was not a need for more hiring.

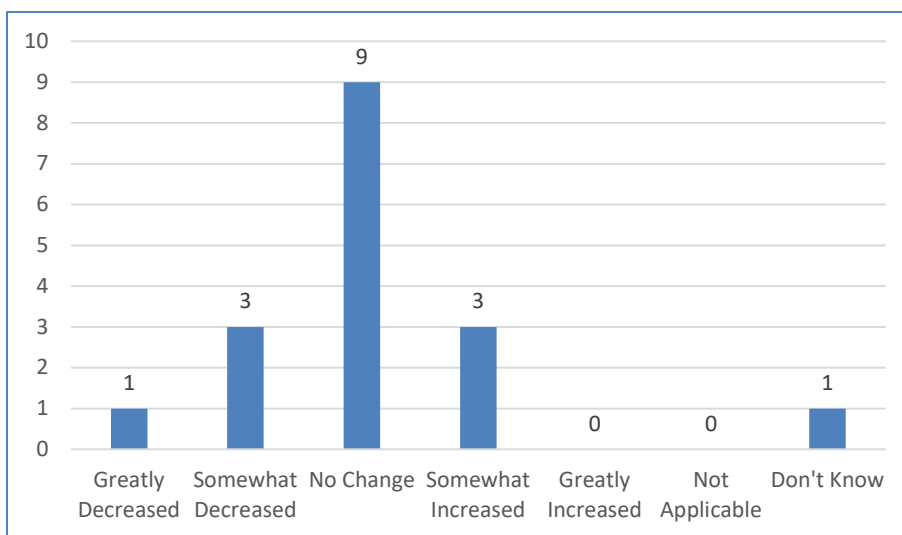


Figure 35. Anticipated employee layoffs in the post-recession

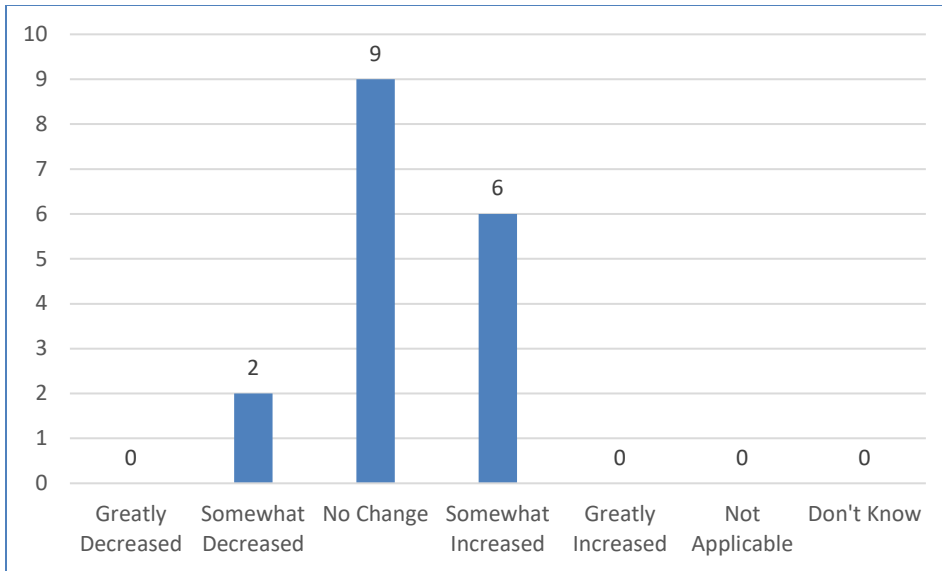


Figure 36. Anticipated filling of vacant positions in county governments in the post-recession

Figures 37-40 illustrate how EDs expect county governments' wages and benefits to change in the near future. Given the long period of recession and the slow recovery, more than half of the EDs anticipate increases in employee wages in the near future. Fewer EDs expect wages to remain the same and two EDs indicated that wages might decline. With rising healthcare costs, county governments expect to transfer some of that cost to their employees, meaning that the share of the total premium and co-pays for health related visits will increase. This is true not just of counties but for almost all levels of governments across the nation (NCSL, 2017). Figure 38 illustrates that the majority of the EDs that responded anticipate a small to large health insurance-related cost-transfer to government employees.

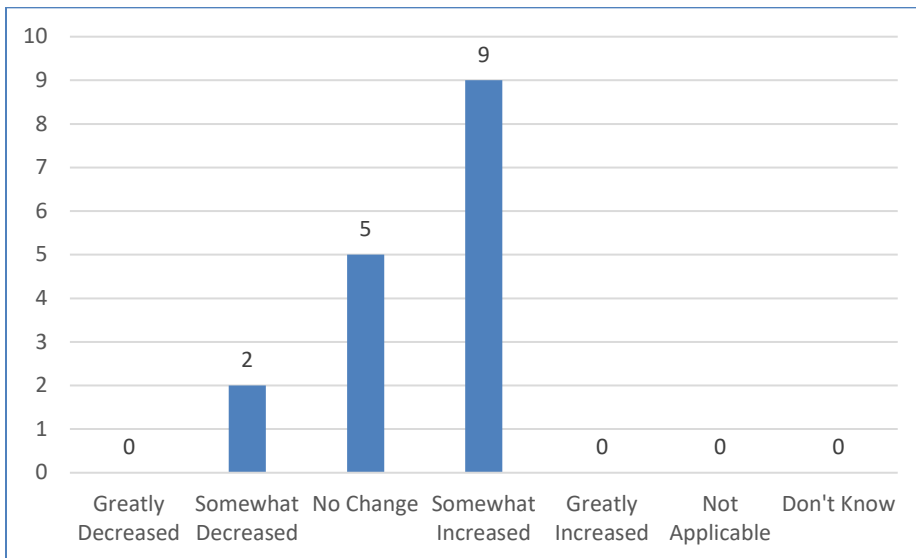


Figure 37. Anticipated employee wages in the post-recession

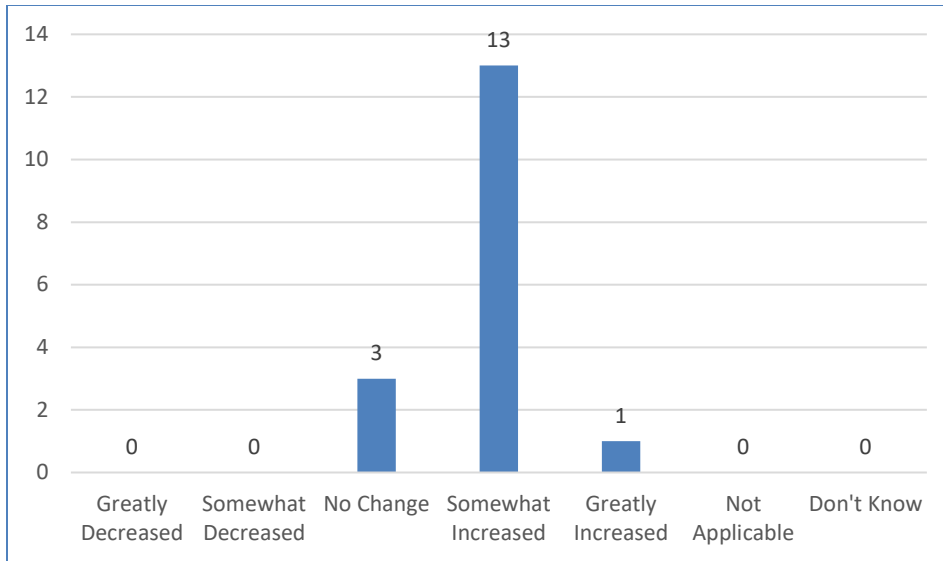


Figure 38. Anticipated employee share of healthcare premiums and co-pays in the post-recession

In comparison, fewer EDs actually expect that retiree’s share of health insurance premiums, deductibles and co-pays will likely increase in the near future. As figure 39 illustrates, more than half of the responding EDs share this sentiment and four EDs expect no changes.

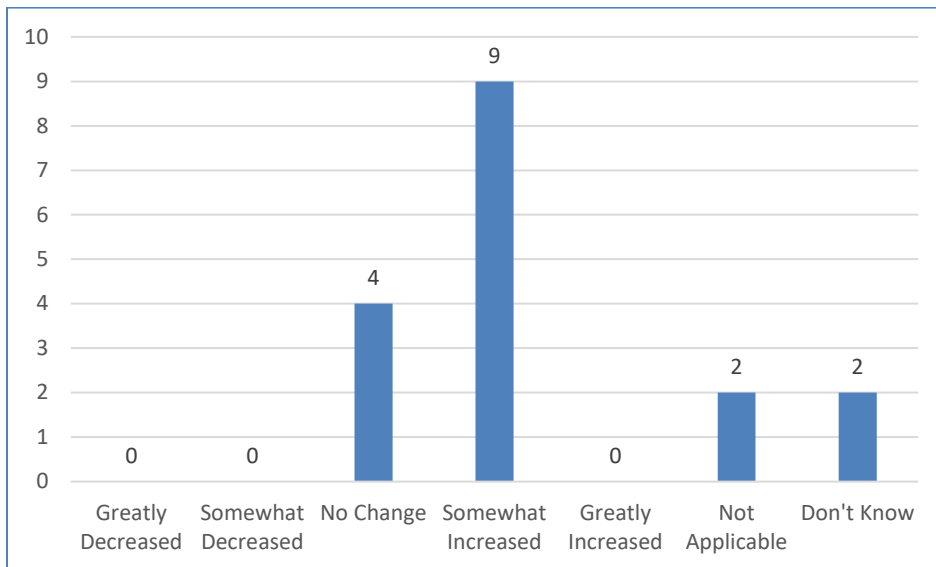


Figure 39. Anticipated retiree share of healthcare premiums and co-pays benefits in the post-recession

As illustrated in Figure 40, more than half of the EDs do not expect an increase in employees’ share of retirement funding and six EDs expect that there will be a marginal increase.

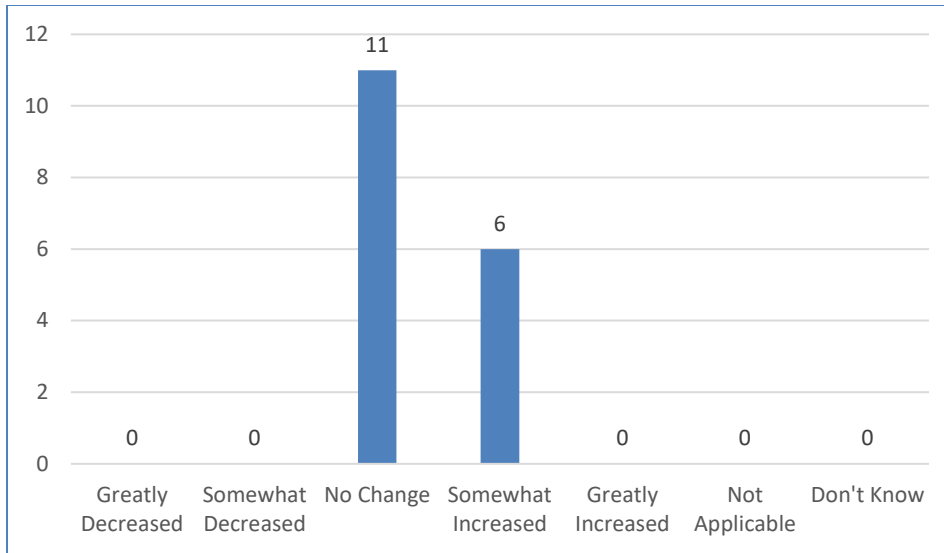


Figure 40. Anticipated employee share of contributions in retirement funds in the post-recession

***Fund balance planning and liquidity***

Ending fund balance refers to the ending balance (revenues over expenditures) of both the governmental and proprietary accounts. Government Accounting Standards Board 54<sup>3</sup> identifies the following types of ending balance: non-spendable, restricted, committed, assigned, and unassigned. A local government should have a positive fund balance and sufficient monies in the unassigned category to ensure that it is able to draw from this account in the event of a situation that warrants added expenditures.

Tables 41 and 42 illustrate the size (relative to expenditures) and expected reliance on ending fund balances of counties during the period following the recession. Interesting, a majority of the responding EDs anticipate county governments to rely more on general fund balance (Figure 41), despite the nation’s recovery from the recession. Further, six EDs indicated that there would be no change in the reliance of county governments on unrestricted and restricted fund balances.

<sup>3</sup> <http://www.gasb.org/st/summary/gstsm54.html>



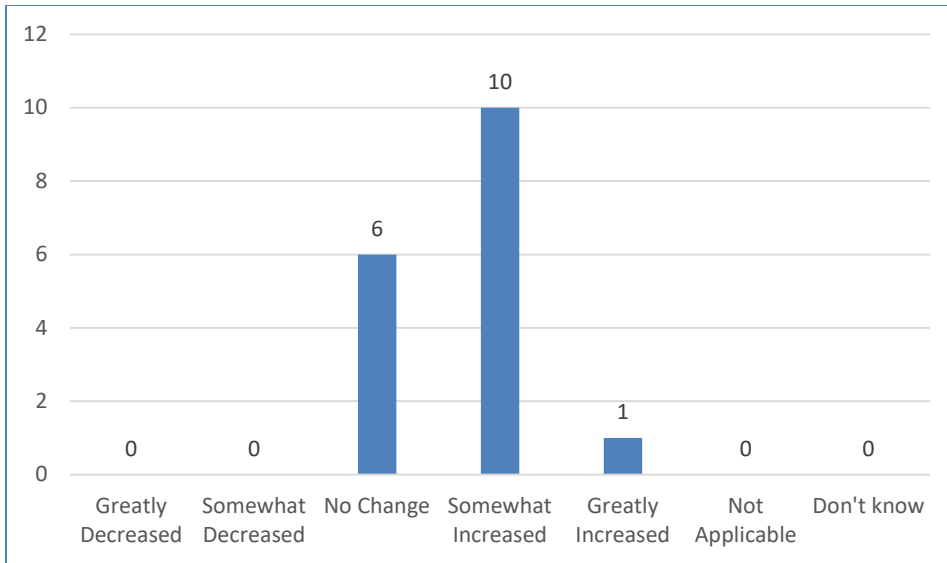


Figure 41. Anticipated reliance on general fund balance in the post-recession

***Unreserved/unassigned general fund balance as a percentage of general fund expenditures***

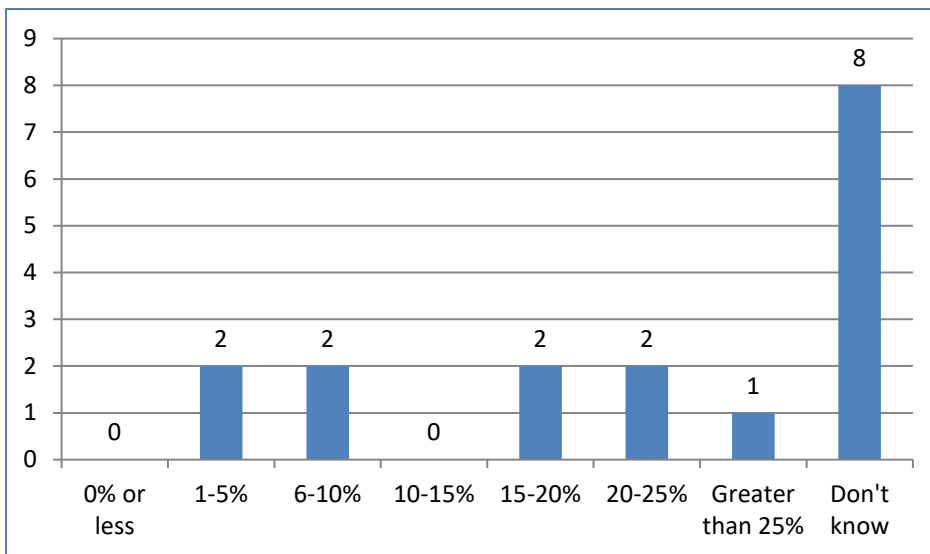


Figure 42. Unassigned fund balances in the post-recession

Ending fund balance refers to the ending balance (revenues over expenditures) of both the governmental and proprietary accounts. Governmental Accounting Standards Board ((GASB) 54, 2017) identifies the following types of ending balance: non-spendable, restricted, committed, assigned, and unassigned. A local government should have a positive fund balance and sufficient monies in the unassigned category to ensure that it is able to draw from this account in the event of a situation that warrants added expenditures. A decline in unassigned fund balances as a percentage of operating revenues over time suggests the government is less able to withstand financial emergencies. Based on the responses (Figure 42), a number of EDs are unaware of the exact state of rural counties in relation to their unassigned fund balances. Nine EDs responded

that the county governments did set aside a percentage, ranging from 1%- more than 25% in the unassigned fund.

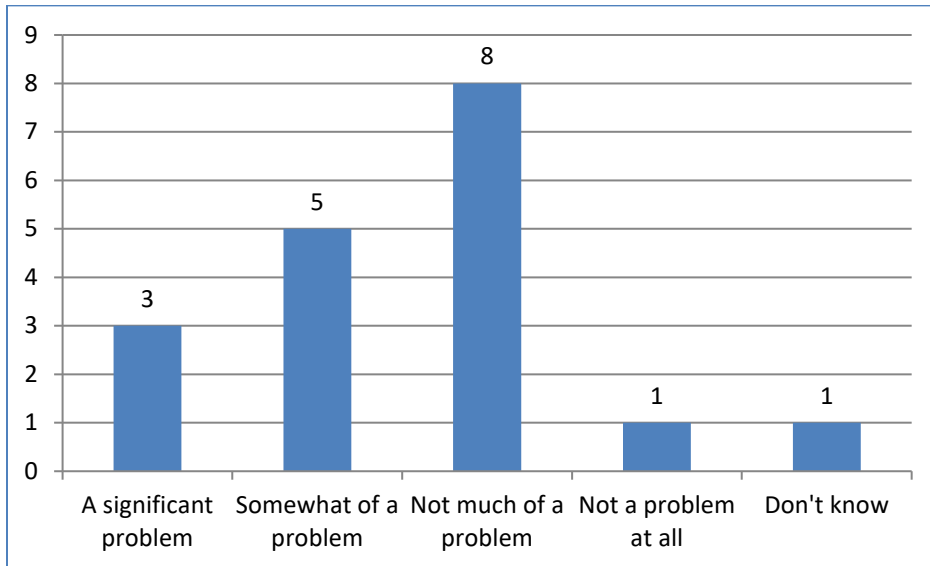


Figure 43. Cash Flow of rural counties in the post-recession

In simple terms, cash flow refers to in inflow and outflow of dollars, into the government accounts from the various revenue generating services and out of it in the form of payments for various types of inputs and wages that allow it to provide different types of public and semi-public services. It is a sign of good fiscal health and as illustrated in figure 43, in the post-recession, half of the EDs reported that as not much of a problem. However, the rest of the responding EDs suggested it was either somewhat or a significant problem.

### *Extent of Recovery since last recession*

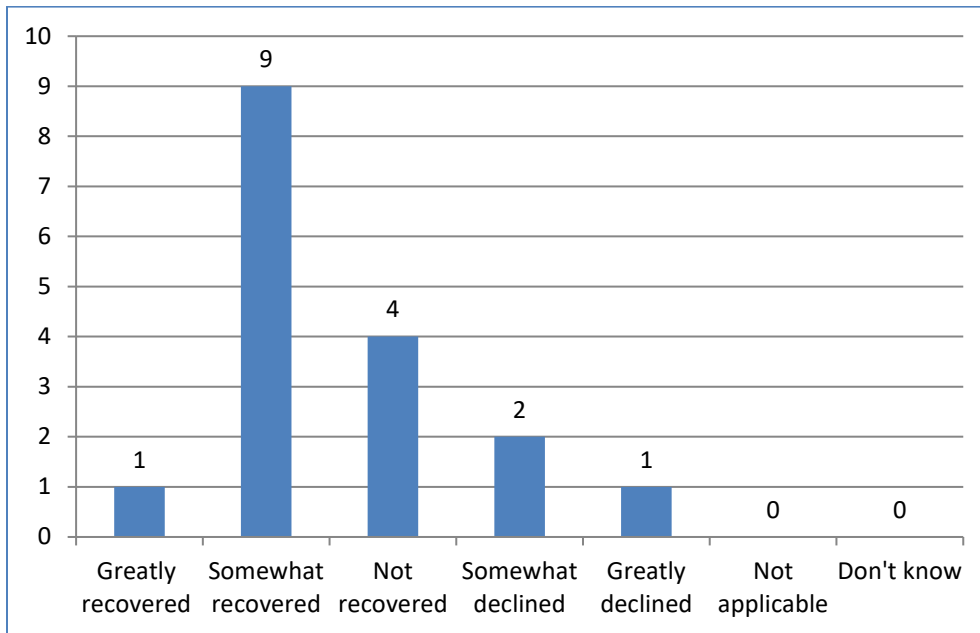


Figure 44. Economic recovery of rural counties in the post-recession

With the recession officially ending in 2010, the survey was conducted almost 5 years later. The responses suggest that the economic recovery has been sporadic with 10 of the 18 EDs reporting general improvement in the economic environment (Figure 44). Three EDs reported having their economies somewhat or greatly diminished. The recovery was partially dictated by the economic sectors that were prominent in various regions across U.S. Regions that rely on production-oriented industries likely experienced much slower recovery compared to regions where service related businesses dominate. Given the variance in economic structure among states, a more robust conclusion about the factors driving recovery would require additional data.

## ***Highlights of Survey Interviews***

*Thinking about state-local government fiscal relations, what do you think are the most important state policies that have negatively impacted county government fiscal conditions?*

In response to this question, researchers noted an overall uniformity across states, with many EDs identifying the same or very similar concerns, especially in relation to the notion of local control and unfunded mandates.

At the same time, there was considerable within-state variation, frequently along the lines of rural versus urban concerns, sometimes described as “red” versus “blue” legislative perspectives. Given these generalizations, there were a number of state-local fiscal policies the EDs identified as problematic.

### ***Disconnect***

There seems often to be a fundamental disconnect between state legislators and local officials. From the county perspective, state legislators often do not understand the needs that exist at the local level and do not trust local legislators to behave in fiscally responsible ways. Because of this, states impose various forms of tax and expenditure limitations that constrain local choice and options. For their part, local officials are simultaneously afraid of their anti-tax local constituents, and/or willing to explain to their voters the needs that exist and do what they feel may be necessary. Mostly, they want greater flexibility and choice.

### **Residual Economic Effects**

There may be a residual effect dating back to the Great Recession. States often took drastic measures in response to their own budget shortfall. This frequently came in the form of dramatic cuts in state aids and/or pushing many unfunded mandates onto counties. Now that the economy is in recovery, states have not made the counties whole, with many aid programs gone or sharply reduced from previous levels. States seem to continue to abdicate what had formerly been their responsibility, often forcing counties to fill the gap. Yet, states insist on constraining local government capacity to respond.

### **Local Control**

Local officials generally seek a greater level of autonomy in managing local affairs. They often chafe at what they perceive as mandates that may constrain choices or compel action. Many local officials believe the best solutions to community problems are found at the local level rather than dictated from a state capitol.

### **Tax and Expenditure Limitations**

Closely related to the issue of local control, local officials similarly object to the various tax and expenditure limitations many states impose. While these controls take many forms, they are almost uniformly disparaged as impinging on local control and constraining local autonomy and choice.

### **Unfunded Mandates**

Many EDs reported that state legislatures had issued edicts mandating new local service responsibilities without providing any additional financial assistance. Similarly, some states withdrew assistance or service provision, effectively transferring responsibility to local government. Within the context of overarching tax and expenditure limitations, this forced reduction of other services or left other needs unmet.

### **Eroding Tax Base**

State legislatures have been exempting an ever-increasing number of tax classes that are important sources of local government revenue. They have exempted entirely or deferred taxation on multiple classes of real property from the property tax roles in the name of economic development or energy production. They have exempted classes of purchases and activities from sales taxes. They have modified fees associated with real estate transactions. Industry sectors and individual businesses seek tax breaks each legislative session with a resulting erosion of the already-limited tax base available to counties.<sup>4</sup>

### **Natural Resource Dependence**

Counties in mineral-rich states have generally done well in recent years. In these states, however, there is some anxiety about the recent drop in demand for oil production, which is affecting state and local revenues. A similar concern is expressed in coal-producing regions, particularly in the eastern U.S.

### **Conversely, what do you think are the most important state policies that have positively impacted county government fiscal conditions?**

Policies positively affecting local fiscal conditions tended to be idiosyncratic and state-specific. While the complaints tended to be much more general in nature, actions on the positive side of the ledger were much more dispersed.

Largely, the EDs felt that states have done very little in recent years to help the counties. There have been some modest enhancements of various types of revenues, e.g. gas tax, motor vehicle registration fees, or severance taxes, but nothing coming near the needs counties have. States have done several one-time initiatives to help with road and bridge or emergency dispatch, but have offered no enduring aid programs. Any significant local government assistance programs cited reflected actions taken many years before.

### **Targeted Aids**

Several states have provided additional assistance to local governments in targeted ways. Examples included transportation, emergency dispatch, and road and bridge funding. In several instances, states enhanced their own fiscal position with the intention of offering additional services providing indirect benefits to counties.

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<sup>4</sup> It should be noted that while local governments may decry state legislatures' exemption of tax base, they will themselves give away tax base in the name of local economic development.

### **One-time Funds**

A number of the EDs interviewed reported that states had replaced shared revenue aid programs with one-time funding programs. For example, states may have replaced ongoing road and bridge aid with a pot of money available by application and distributed prioritizing greatest need or impact.

### **Gas Tax Increases**

A number of states have used lower oil and gas prices to increase gas taxes modestly, sharing some of the revenue with local governments.

### **Energy States**

A handful of states implemented policies to help rural counties with transportation funding, economic development assistance and some aid. In oil-rich states, several have expanded state funding assistance for services. This was particularly true in states where communities had experienced very rapid growth, outpacing the local capacity to meet law enforcement and social service needs.

**Over the past 1-2 years, have there been any significant changes in state aids to county governments? If so, what areas of county government operations do these impact?**

### **Mostly Cuts**

In the majority of interviews, EDs were critical of their state legislatures, citing cuts in transportation funding, public health and mental health funding, education, and pension obligations. Most repeated many of the examples cited in Question #8. Other state directors cited the reduction, elimination, or the total absence of state aid.

Rarely, states have approved new local option revenue sources, but frequently require public approval. Many local officials are loathe to face constituents with new funding requests especially in difficult economic times for their citizens.

**What do you consider to be the top 3 issues facing rural counties in your state now? Describe.**

### **Economic Opportunity**

The greatest overall need that exists in rural areas is the lack of economic opportunity leading to population loss and a declining local tax base to support local public finances. Associated with the population loss and aging of the population base is a growing leadership crisis where there just is not the replacement for the leadership and volunteers needed to keep rural communities vital and functioning.

### **Infrastructure**

There are growing needs related to infrastructure. This includes roads & bridges, water and wastewater, and schools. There simply are not sufficient local resources to deal with the scale of the needs, state aid is deficient, and there is not sufficient authority and flexibility to respond independently.

### **Population Movement**

In several states, EDs reported the population migration had created problems. Out-migration from some rural areas has left aging infrastructure and an insufficient population base. Rapid in-migration to amenity-rich areas was overwhelming inadequate or nonexistent infrastructure and public services. Several EDs cited the environmental consequences of population growth.

### **Service Reorganization**

Several trends are occurring that are creating greater levels of local need. Several EDs cited their states' choice to forego expanding Medicaid funding leading to growing local health and human service's needs. Similarly, mental health reform keeps individuals in their communities rather than state facilities. In these instances, greater need for services is arising at the local level, and the states are helping too little or not at all. Law enforcement needs were also cited. Movement toward community-based service and treatment was cited in relation to prison-sentencing reform that will keep more offenders in the community.

### **Health and Education**

Two service areas frequently identified as challenging for rural areas were health and education. The need for health and mental health services was growing faster than state and federal assistance. Many rural hospitals are no longer financially viable without public subsidy.

Maintaining the local school system also has challenged many rural communities. Buildings, equipment and technology were antiquated and there was insufficient local capacity to upgrade or improve.

**Based on your knowledge about how rural counties in your state have responded to fiscal stress they may have experienced in recent history, can you think of instances where county officials have responded with creative approaches to partially or completely mitigate the impacts? If so, can you identify which counties and describe the actions they have taken or the programs they have put in place. We may contact them to get additional details.**

EDs were hard-pressed to cite many examples of local government innovation. Most frequently cited was a trend toward regionalization, formal consolidation, or informal cooperation. In the realm of regionalization, several mentioned mental health. Other examples included economic development, regional public health, and regional jail facilities. In terms of consolidation/cooperation, several mentioned combined emergency dispatch services, and solid waste management.

## Conclusions

The survey helped reveal how the Executive Directors of state county associations observe rural county officials responding to the financial challenges in the period following the Great Recession in 2007-08, and how they perceive their current fiscal situation. In addition, the study focused on how county officials, especially in rural areas, anticipate dealing with their fiscal situation in the immediate future (2017 and beyond). The survey provided an understanding of the issues and circumstances facing different states, and how county officials are dealing with revenue generation, revenue-sharing, tax and expenditure limitations, as well as and innovative approaches to dealing with fiscal challenges.

With a response rate of 36 percent, six broad themes are evident from the findings of the quantitative survey – revenue trends, intergovernmental fiscal relations, community needs, long-term investments and debt, public employee wages and benefits, fund balance situation, and liquidity situation of counties. Findings reveal that county revenues were impacted in two distinct ways – some states increased while others stayed the same or declined, likely based on how each area recovered from the recession. This was the case with property tax, sales tax, and user fees. In addition, select drivers of revenue changes like population growth, tax delinquencies and home foreclosures also showed various trends. In terms of the expectation for the immediate future, most state EDs expect either no change or some increase in property tax rates. About half of the EDs, those in states that have a sales tax in place, expect an increase in sales tax rates. More states do not anticipate changes to user fees and charges while fewer states expect marginal increases.

In terms of federal aid to states, half of the responding EDs expect no change while the rest anticipate a decrease in aid from the federal government. Almost all the EDs reported that state aids declined marginally or greatly. In the post-recession, about half of the responding EDs did not report counties securing any additional debt while six EDs saw increase in borrowing. Similarly, a number of EDs reported increases in infrastructure spending which are typically funded through external borrowing.

In the post-recession era, community needs in public safety, infrastructure, human services, and general government operations were reported to have increased. Consistent with that, actual spending in public safety and general government operations also increased. Economic development spending, however, remained flat according to most of the responding EDs.

In an effort to control spending, counties in a few states privatized or contracted services. More than half of the responding EDs witnessed reduction in the numbers of county employees. Several reported stable levels of employment and only two EDs reported rural counties hiring additional employees. Seven EDs witnessed increases in wage rates while eleven EDs reported no change or marginal decline in wage rates. Pension and other retirement obligations increased in three states, declined in three states and remained the same in the majority of the states. In almost all the states that responded, the cost of health benefits increased marginally or greatly. Half of the responding EDs witnessed actual increases in human services expenditures and half reported no change or marginal declines. Cost-sharing between county governments was prevalent in eleven states indicating that as an effective way of reducing administrative and



service delivery costs. A majority of state EDs reported county hiring freezes but few counties shed existing employees. Employee shares of premiums and co-pays for health insurance increased in most of the states. In retirement contributions, more EDs reported no change and in six states, there was an increase.

The ending fund balance for counties in the post-recession improved in ten states and remained the same in six states. In almost an identical trend, the reliance on these 'rainy day' funds also increased and remained the same in similar number of counties. While half of the responding EDs reported cash flow as either somewhat or a significant problem, the rest reported it as not much or not at all a problem.

On the broad question of the extent of economic recovery, ten state EDs responded having somewhat or greatly recovered. The rest were split between having not recovered or somewhat or greatly declined. This is in line with some of the findings from another study that was conducted about the same time by the National Association of Counties (NACO, 2016). While it is apparent that the recession played a significant role in rural counties' financial condition, it is also apparent, based on the interviews that political dynamics at the state level often aggravated the situation. For instance, several states have been unable to approve budget. This had practical consequences for local governments who were already faced with challenging fiscal conditions. Further, mandating tax and spending limitations also made it extremely difficult for counties to deal with the difficult fiscal situation (Stallman et al., 2017). While there was generally broad consensus on the need for making investments in infrastructure improvements, how that would be funded did not find the same level of agreement at the state and local level. Cost-sharing was also another aspect that impacted state and local government relations. In many states there were concerns that the state government was either not compensating counties adequately for carrying out the state functions or in some instances was forcing counties to bear the cost of state-level services of which they were not direct beneficiaries.

Unfunded mandates were observed to be a problem as it relates to state and local government relations. The growing disconnect between state and local officials as it relates to understanding the needs at the local level was identified as contributing to the counties' fiscal challenges. In addition, states, by exempting sectors from taxation, while aimed at economic development, were eroding the tax base of county governments. On a positive note, some states reported that by allowing for additional revenues via gas tax, motor vehicle registration fees and severance taxes, counties had benefitted. Some states also had benefitted counties by way of one-time funds or targeted aid programs offered by states in specific sectors.

Most respondents identified state aid funding cuts triggered by the great recession as having a lasting impact on counties, especially in rural areas. Providing economic opportunities to its residents, maintaining existing infrastructure dealing with depopulation, health and education funding and different types of service reorganization in terms of how it is funded or organized for delivery.

## Recommendations Relating to Local Fiscal Policy

Local financial management is becoming increasingly complex. The responsibilities of local governments continue to grow, while public service expectations remain high. This challenges governments to raise sufficient revenues while controlling their expenditures.

### Revenues

Four major revenue sources are within local control: property taxes, sales taxes, user fees, and intergovernmental transfers and aids. Each presents its own challenges.

County governments remain highly dependent on property taxes as a revenue source. But, increasing public dissatisfaction with the property tax is forcing counties to find other ways to fund local services.

Imposing or increasing a local sales tax is often greeted with opposition from citizens and the local business community based on fears that it may adversely affect retail competitiveness. Combining the sales tax with efforts to foster a healthy environment for business activity may reduce opposition and benefit county revenue by boosting both retail sales and sales tax revenues.

While their use is still somewhat limited, user fees are becoming an increasingly important revenue source for some counties. As user fees apply to only the beneficiaries of a service, they can be a fair and efficient way to finance public services. Of course, there must always be a distinction between services subject to user fees and those that should be available to all citizens regardless of their ability to pay.

Many intergovernmental transfers and aids are formula-based, but others rely on local initiative. Grant funds are often available from the state and federal government for communities that go through an application process. Such applications, however, typically require a serious commitment of local resources and, if successful, provide funding for only a limited period of time. Many rural counties may not have the personnel and other resources to complete the application process.

Generally, a local government should use a revenue mix that provides adequate, stable funding without placing an unfair burden on any particular group. There is no universally optimal mix, however. It depends on local needs, preferences, and resources. The following should be considered when evaluating local revenue sources:

**Adequacy:** Is the revenue source regular, reliable, and not susceptible to economic change?

**Adaptability:** Can rates be easily adjusted to meet changing needs and avoid shortfalls?

**Administrative ease and economy:** Is it simple and inexpensive to administer?

**Economic effects:** How does it affect local resource use and growth?

**Social acceptability:** How do citizens and businesses perceive the tax?

**Fairness:** Does it treat people uniformly and conform to social definitions of fairness, such as ability-to-pay? Do those who benefit the most pay the most?

## **Expenditures**

Controlling expenditures is also an important component of local fiscal policy, as it helps keep taxes low. It should, however, be done with the level of service local government wants to provide in mind. Performance standards provide a means for local governments to ensure that a given level of expenditure is accomplishing their goals. Several strategies for controlling local expenditures are outlined below.

Cutting spending is, perhaps, one of the more obvious means of controlling expenditures. It is often very difficult, however, because it generally means reducing or eliminating services for certain constituents and inevitably affects local government employees. Some options include:

- Cutting programs across-the-board;
- Cutting programs selectively;
- Subcontracting operations, services, and programs;
- Offering early retirement;
- Reducing work hours, Redefining departments and jobs; and
- Increasing worker productivity through training and technology

The above list does not imply that all of the options are equal in their outcomes. Counties, at times, attempt to reduce current spending by delaying infrastructure maintenance. This method generally proves ineffective, however, as rebuilding or replacing infrastructure is typically far more costly in the long-term than regular maintenance.

Changing the way services are provided is another means of controlling local expenditures. Privatizing services may make sense, but should be done only after careful study. Other alternatives include: public-private partnerships, collaborating with other units of local government, consolidating, and using local volunteers. While these strategies can be effective in certain circumstances, they require careful planning and feasibility analysis.

Long-term planning during budgeting can also help local governments control their expenditures. Planning means anticipating future needs, the timing of expenditures, and the total cost of projects and is particularly important for new development and capital expenditures. A capital improvements plan is useful to anticipate the order, timing, and financing of capital expenditures.

Effectively using debt is another strategy for controlling local government expenditures. Governments use debt primarily for long-term infrastructure investment. This amortizes costs over the life of the investment, reducing the immediate financial burden and allowing future beneficiaries to pay their share. Debt should never be used to reduce current property taxes. Financial advisors are available to assist local governments in their use of debt.

## **Fiscal Management**

To be effective, fiscal management must be a regular part of local government operations. Tracking monthly revenues and expenditures is vital. Regular monitoring and immediate action throughout the year will reduce budgetary stress. Investing idle funds where they yield the greatest return is appropriate as long as the investments are safe and funds available when needed. Fiscal impact studies can help avoid unexpected costs. These studies anticipate all costs (direct and indirect) associated with a project. Perhaps most importantly, policymakers should regularly and formally discuss fiscal issues, evaluate current policy, and consider policy alternatives. A proactive, long-term approach helps to ensure quality services, low taxes, and fiscal stability for current and future generations.

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## Appendix

### Two-part survey used for the study

A team of researchers from several Midwestern public universities (Iowa, Kansas, Michigan, Missouri, and Nebraska) is conducting a national survey of the Executive Directors of all NACo-affiliated state Counties' Associations to better understand the issue of fiscal stress being experienced by county governments across the nation. The objectives of the study are to:

- (1) enhance understanding of the current state of county fiscal conditions and any fiscal stress that may exist;
- (2) identify innovative local response strategies to fiscal challenges;
- (3) better understand state policies influencing state-local inter-governmental fiscal relations;
- (4) create state-policy data variables that may be useful for public finance research;

As the Executive Director of your state Counties Association, we believe you are uniquely qualified to represent the perspectives of the counties in your state. Individual responses collected through this survey will be confidential.

This research study has been reviewed by the Institutional Review Board at Iowa State University. For research-related questions or concerns regarding subjects' rights, you can contact the University's Compliance Coordinator, at [redacted] or email [redacted]. Your decision whether or not to participate will not affect your current or future relations with Iowa State University or any other agency of the state. If you decide to participate, you are free to refuse to answer any of the questions. You can withdraw at any time without your relations with the university being affected. You can contact Biswa Das, the Principal Investigator by phone (515) 509-9603, or email [bdas@iastate.edu](mailto:bdas@iastate.edu) if you have any questions about the survey or how the results will be utilized.

The survey will be done in two parts. The first part which will be an online survey consists of questions that have objective responses. We will be sending an email with the link to the website where you will be undertaking the online portion of the survey. The online portion of the survey will take approximately 20 minutes of your time for which we would like to thank you.

For the second part, the survey will consist of open ended questions. We are sending this questionnaire in advance so you can see the questions that will be asked and can reflect on the situation in your state's counties. We will be making a telephone call that will be scheduled with you ahead of time. The telephone part of the survey will be for approximately 15-20 minutes.



## Part I. Understanding Fiscal Stress in Rural Counties

1. For how long have you held the position of Executive Director of your state county association?

\_\_\_\_\_ Years

The USDA Economic Research Service defines ‘rural’ to mean counties that have a population less than 50,000. These are the counties we would like you to reference as you answer these questions.

2. Thinking about the financial needs of rural counties in your state following the last big recession, would you say that they have been less able or better able to meet their financial needs?

### Check One

- \_\_\_\_\_ Significantly Less Able  
\_\_\_\_\_ Somewhat Less Able  
\_\_\_\_\_ Neither Less nor Better Able  
\_\_\_\_\_ Somewhat Better Able  
\_\_\_\_\_ Significantly Better Able  
\_\_\_\_\_ Don’t Know

3. Based on your understanding of the rural counties in your state, please consider the ways the following county government characteristics have changed following the last big recession. Indicate whether — in your opinion — there has been a decrease, an increase, or no change during the past few years.

For each item, please assign a score using the following scale:

- 1 = Greatly Decreased  
2 = Somewhat Decreased  
3 = No Change  
4 = Somewhat Increased  
5 = Greatly Increased  
6 = Not Applicable  
7 = Don't Know

### Score

- \_\_\_\_\_ Revenue from property taxes  
\_\_\_\_\_ Revenue from fees for services, licenses, transfers, etc.  
\_\_\_\_\_ Revenues from sales tax  
\_\_\_\_\_ Amount of debt  
\_\_\_\_\_ Ability to repay debt  
\_\_\_\_\_ Amount of federal aid  
\_\_\_\_\_ Amount of state aid

- \_\_\_\_\_ Tax delinquencies
- \_\_\_\_\_ Home foreclosures
- \_\_\_\_\_ Population
- \_\_\_\_\_ Public safety needs
- \_\_\_\_\_ Infrastructure needs
- \_\_\_\_\_ Human service needs
- \_\_\_\_\_ General government operations needs
- \_\_\_\_\_ Number of employees that work for county governments
- \_\_\_\_\_ Pay rates for employee wages and salaries
- \_\_\_\_\_ Properly funding pensions and other retiree obligations
- \_\_\_\_\_ Cost of current employee health benefits
- \_\_\_\_\_ Cost of retired employee health benefits

4. Comparing the period following the last big recession to the next fiscal year, please indicate which actions rural counties are most likely to take.

For each item, please assign a score using the following scale:

- 1 = Greatly Decrease
- 2 = Somewhat Decrease
- 3 = No Change
- 4 = Somewhat Increase
- 5 = Greatly Increase
- 6 = Not Applicable
- 7 = Don't Know

**Score**

- \_\_\_\_\_ Property tax rates
- \_\_\_\_\_ Sales tax rates
- \_\_\_\_\_ New sales or use taxes
- \_\_\_\_\_ Charges for fees, licenses, etc.
- \_\_\_\_\_ Reliance on general fund balance
- \_\_\_\_\_ Reliance on “rainy day” funds
- \_\_\_\_\_ Amount of services provided
- \_\_\_\_\_ Actual public safety spending
- \_\_\_\_\_ Actual infrastructure spending
- \_\_\_\_\_ Actual human services spending
- \_\_\_\_\_ Actual general government operations spending
- \_\_\_\_\_ Funding for economic development programs
- \_\_\_\_\_ Amount of debt
- \_\_\_\_\_ Sale of public assets (i.e., parks, buildings, etc.)
- \_\_\_\_\_ Privatizing or contracting out of services
- \_\_\_\_\_ Number and/or scope of inter-local agreements or other cost-sharing plans with other governments
- \_\_\_\_\_ Workforce hiring
- \_\_\_\_\_ Workforce layoffs
- \_\_\_\_\_ Not filling vacant positions

- Employee pay rates
- Employees' share of premiums, deductibles, and/or co-pays on health insurance
- Employees' share of contributions to retirement funds
- Retirees' share of premiums, deductibles, and/or co-pays on health insurance

5. Different local jurisdictions manage their unreserved/unassigned general fund balances in different ways depending on their specific circumstances. Despite these differences, we're interested in understanding the overall changes in these balances over time. Approximately what was the rural counties' unreserved/unassigned general fund balance as a percentage of general fund expenditures at the end of its last fiscal year?

**Check One**

- 0% or less
- 1-05%
- 06-10%
- 10-15%
- 15-20%
- 20-25%
- Greater than 25%
- Don't Know

6. In your opinion, is your states' rural counties' cash flow and their ability to pay bills in a timely manner a

A significant problem   Somewhat of a problem   Not much of a problem   Not a problem at all   Don't Know

7. Overall, based on your understanding of the rural counties in your state, how would you characterize the extent to which they have recovered from the last recession?

Please assign a score using the following scale:

- 1 = Greatly recovered
- 2 = Somewhat recovered
- 3 = Not recovered
- 4 = Somewhat declined
- 5 = Greatly declined
- 6 = Not Applicable
- 7 = Don't Know

## **Part II. State Policies and State/Local Fiscal Relations (open ended)**

8. Thinking about state-local government fiscal relations, what do you think are the most important state policies that have negatively impacted county government fiscal conditions? Please name the policy and describe its impact. Please indicate how significant it is/will be in affecting local governments' fiscal condition.
9. Conversely, what do you think are the most important state policies that have positively impacted county government fiscal conditions? Please name the policy and describe its impact. Please indicate how significant it is/will be in affecting local governments' fiscal condition.
10. Over the past 1-2 years, have there been any significant changes in state aids to county governments? If so, what areas of county government operations do these impact?
11. What do you consider to be the top 3 issues facing rural counties in your state now? Describe.
12. Based on your knowledge about how rural counties in your state have responded to fiscal stress they may have experienced in recent history, can you think of instances where county officials have responded with creative approaches to partially or completely mitigate the impacts? If so, can you identify which counties and describe the actions they have taken or the programs they have put in place. We may contact them to get additional details.

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