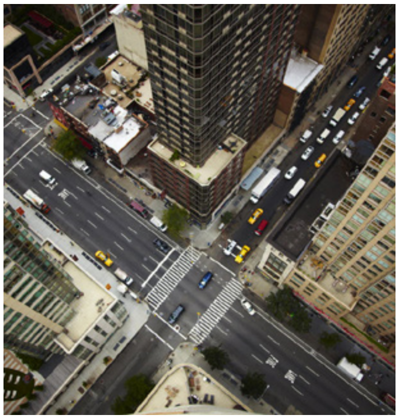

America's Big Cities in Volatile Times

Meeting Fiscal Challenges and Preparing for the Future

NOVEMBER 2013

The Pew Charitable Trusts is driven by the power of knowledge to solve today's most challenging problems. Pew applies a rigorous, analytical approach to improve public policy, inform the public, and stimulate civic life.

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This research benefited tremendously from the insights and expertise of five external reviewers: Joseph Cortright, president and principal economist, Impresa; Mark Funkhouser, director, Governing Institute; Matt Nagle, senior policy analyst, Indiana University Public Policy Institute; Andrew Reschovsky, professor emeritus of public affairs and applied economics, Robert M. La Follette School of Public Affairs, University of Wisconsin, Madison; and Lisa Washburn, managing director, Municipal Market Advisors. These experts provided feedback and guidance at critical stages in the project. Although they have screened the report for accuracy, neither they nor their organizations necessarily endorse its findings or conclusions.

Acknowledgments

We would like to thank Larry Eichel for his early guidance and thoughtful feedback throughout this research process. Valuable research support was provided by Jennifer Gelman, Liz Gross, Vicki Kleger, and Abigail Sylvester. We would like to thank our following colleagues for their insights and guidance: Samantha Chao, Gabrielle Cosel, Erin Currier, Camille Galdes, Maria Ho, Jane Koppelman, Jeremy Smith, Ingrid Stegemoeller, and Rachel Zetts. We also thank Dan Benderly, Lauren Dickinson, Jennifer V. Doctors, Sarah Leiseca, Jeremy Ratner, Ed Paisley, Fred Schecker, and Natalia Pelayo for providing valuable feedback and production assistance on this report. In addition, we thank the many city officials and other experts in the field who were so generous with their time, knowledge, and expertise.

For additional information, visit http://www.pewstates.org/cities.

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Overview

The Great Recession created fiscal challenges for the 30 cities at the centers of the nation's most populous metropolitan areas that continued well past the recession's official end in June 2009. For most of these cities, the fiscal brunt was borne later than for the national and state governments and recovery has been slow.

Cities dealt with fiscal strain in a variety of ways: dipping into reserve funds, cutting spending, gaining help from the federal or state governments, and increasing revenue from tax and nontax sources. Although these strategies offered short-term solutions, many cities still faced declining revenue in 2011, the consequence of reduced spending, shrunken reserves, and rising pension and retiree health care costs.

Property taxes, which can be slow to respond to economic swings, helped delay the early fiscal effects of the Great Recession for most of these cities, but they began to decline in 2010, reflecting a deferred impact of the housing crisis. This trend was compounded by increasingly unpredictable aid from states and the federal government that were dealing with their own budgetary constraints.

Researchers from Pew standardized data from the Comprehensive Annual Financial Reports from 2007 through 2011, the latest year of complete data available, for all of these 30 cities. This report examines key elements of each city's fiscal conditions, including revenue, expenditures, reserves, and long-term obligations, and adjusted them for inflation to facilitate comparison across the years. These adjustments allow insight into fiscal trends across cities and over time. Direct comparisons between cities may be limited, however, by differences in cities' tax structures and the range of services each city provides. (See Appendix for analysis methodology.[1])

Although each city had its own distinct experience, looking across all 30 revealed several notable findings. They are examined in depth throughout this report, but they include:

- The 30 cities felt the recession's fiscal effects late: Most hit their lowest revenue in 2010 or 2011, a year or more after the end of the downturn and the low point in revenue for state governments in 2009.
- By 2011, revenue had rebounded to or above previous peak levels in less than one-third of the cities studied. But even those improvements were tenuous because revenue increases in many of these cities were heavily driven by aid from other governments, not by growth in their own revenue streams.
- More than two-thirds of the cities had not recovered to their previous revenue peak by 2011.
- Fluctuations in aid between 2007 and 2011 from the federal and state governments—a source that city policymakers do not control—were the leading factor in 14 cities' revenue declines *and* rebounds.
- Declines in smaller revenue sources—such as income from investments or from the sale or lease of assets, such as parking meters or facilities—played an outsized role in driving budget shortfalls in most cities.
- Property tax collections remained relatively robust until 2010 and 2011. Further projected declines of this key revenue source suggest that cities may face new challenges in coming years.

As cities look ahead, ongoing fiscal constraints at the state and federal levels could further diminish aid to local governments and add to an already shaky fiscal picture. Cities' unfunded retirement obligations put even more ongoing pressure on their finances.

American cities have a significant impact on the economies and long-term prosperity of states and the nation. The 30 cities in this study and their metropolitan areas account for 49 percent of the nation's gross domestic product.[2] Collectively, they have nearly 34 million residents—more than 1 in 10 Americans—with an additional 108 million living in the regions they anchor, and those populations depend on the core functions of municipalities, such as fire and police protection, parks and libraries, and infrastructure investments.[3] Addressing demands for local services, claims on existing revenue from unfunded liabilities, and other commitments with fewer dollars will mean tough choices for local leaders and have serious implications for the national economy.

This report, and the companion profiles and interactive data tool that look at each city's experience, examine how they navigated the worst U.S. economic downturn since the Great Depression and its aftermath. These materials focus in particular on postrecession revenue as compared with earlier peaks; explore future prospects; and consider the likely effects of cities' fiscal struggles and strengths on the economic health of their states and the nation.

Cities' financial challenges continued after the Great Recession ended

Revenue, more than any other factor, drives key fiscal decisions such as how much to spend on police and fire protection and trash pickup, setting aside or drawing down reserve funds, or paying retirement obligations. Two years after the Great Recession's end in June 2009, the 30 large U.S. cities studied by Pew continued to face revenue challenges. (See Figure 1.)

Only nine of these cities had returned to their previous revenue peak by 2011, adjusted for inflation—Atlanta; Chicago; Dallas; Pittsburgh; Portland, OR; San Antonio; San Francisco; St. Louis; and the District of Columbia. But rebounding to prior highs does not necessarily signal a self-sustaining, long-term recovery. Revenue growth can result from policy decisions, such as a temporary tax increase or infusion of one-time aid, even when the underlying revenue base is still weak.[4] For instance, to boost revenue, Atlanta, Boston, and Philadelphia increased property tax rates, and Denver and New York raised sales taxes. A number of other cities, among them Baltimore, Los Angeles, and St. Louis, increased charges and fees. Further, when any city returns to a previous peak, it is only back to where it was before the recession. The city could still be short of what is needed simply to maintain public services because, generally, populations and costs have grown.

These nine cities also relied heavily on intergovernmental aid for revenue recovery. In each, aid from other governments was the first- or second-largest contributor of growth as city revenue recovered from low points. This group of cities typically got larger increases in intergovernmental aid and received infusions from states and the federal government later in the study period—in 2010 and 2011—than did the other 21 cities, which remained below their revenue peaks in 2011.

But for these nine cities, that their revenue rebounds were generated through aid from other governments could mean their recoveries are tenuous. Atlanta's receipts bounced back sharply from their 2009 trough to a new high in 2010, and a $35 million bump in intergovernmental aid was the biggest factor. By 2011, state and federal funds had dropped $21 million from the previous year. As a result, total city revenue fell slightly. Other rebounding cities risk overall revenue declines if intergovernmental aid dips before other revenue sources recover.

FIGURE 1

Cities Experienced Revenue Declines at Different Times During and After the Great Recession

Cities revenue troughs, by year

2008	2009	2010	2011
Washington	Atlanta	Chicago	Boston
	Baltimore	Cleveland	Houston
	Cincinnati	Dallas	Miami
	Denver	Detroit	Minneapolis
	New York	Kansas City, MO	Orlando, FL
	Portland, OR	Las Vegas	Phoenix
	San Antonio	Los Angeles	Sacramento, CA
	San Francisco	Philadelphia	Tampa, FL
	Seattle	Pittsburgh	
		Riverside, CA	
		San Diego	
		St. Louis	

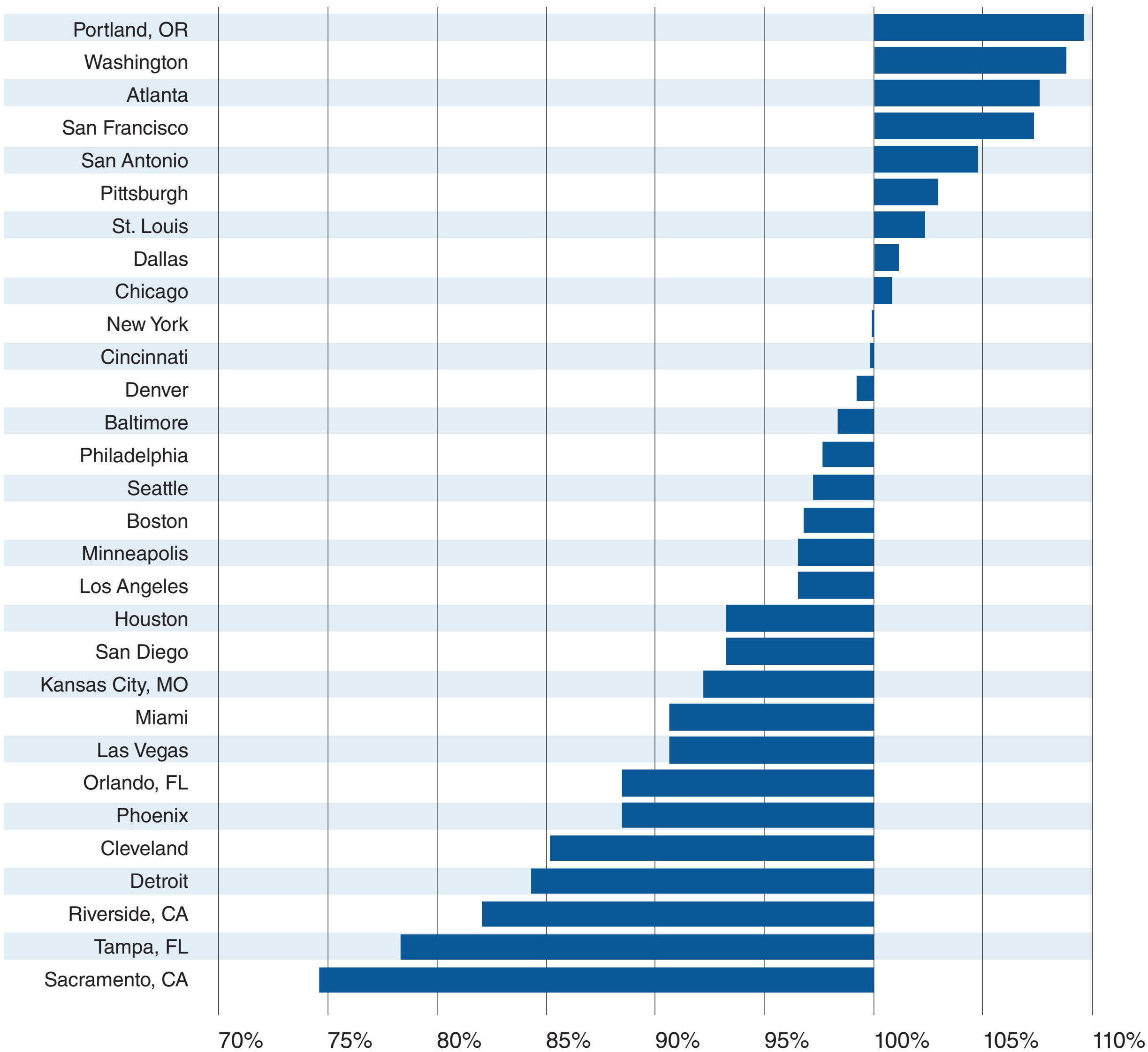
Revenue in 21 cities had not yet returned to peak levels

Two years after the end of the Great Recession, 21 of the 30 cities still had not recovered to their prior revenue peaks. (See Figure 2.) In fiscal 2011, eight of these cities—Boston; Houston; Miami; Minneapolis; Orlando, FL; Phoenix; Sacramento, CA; and Tampa, FL—were at their lowest revenue points.[5] Not only did these cities' revenue show no signs of rebounding, some also were still in decline.[6]

FIGURE 2

Most Studied Cities Had Not Recovered to Prerecession Revenue Highs By 2011

2011 revenue as percent of previous peak, by city



In five of these cities, however—Baltimore, Cincinnati, Denver, New York, and Philadelphia—revenue was growing and, by 2011, approaching previous peaks.[7] No single factor explains why these five cities were closer to recovering their revenue levels than the rest of the 21, which remained at or near their troughs. Increases in property tax collections and nontax revenue, such as investment income, were consistent factors contributing to revenue growth across those five cities, but these sources were not necessarily the key driver of a rebound in each of them. (See Figure 3.)

In Denver, for example, the sales tax, which accounts for about one-third of total governmental income, was the primary factor in the city's overall revenue growth between 2009 and 2011. A 10 percent increase in sales tax collections over these two years—$46 million—brought the city close to previous peak levels in 2011. In Cincinnati, a 13 percent increase in intergovernmental aid between 2009 and 2011—which includes funds from state and federal governments—had revenue again climbing toward its earlier peak.

Among the 16 cities that remained at or close to revenue low points in 2011, declining aid from other governments played a major role in their struggles.[8] Thirteen cities received infusions of intergovernmental aid in 2008 or 2009 that diminished in subsequent years, and revenue fell accordingly when they could not make up the difference with own-source collections.[9]

FIGURE 3

Cities Had Varying Revenue Outlooks in 2011

2011 revenue relative to prior peaks and troughs, by city

Cities Above Peak	Atlanta Chicago Dallas Pittsburgh Portland, OR San Antonio San Francisco St. Louis Washington
2011 Revenue Below Preceding Peak	
Cities Close to Peak	Baltimore Cincinnati Denver New York Philadelphia
Cities Close to Trough	Cleveland Detroit Kansas City, MO Las Vegas Los Angeles Riverside, CA San Diego Seattle
Cities Still Declining	Boston Houston Miami Minneapolis Orlando, FL Phoenix Sacramento, CA Tampa, FL

What caused revenue challenges?

Revenue challenges across the 30 cities were not caused by one single factor, because structures and economies vary widely. Although each city's fiscal experience was unique, Pew found two causes of falling revenue in more than 20 of the cities. Intergovernmental aid drove revenue declines in nine cities. And, surprisingly, smaller revenue sources—such as investment income, charges and fees, and smaller taxes, such as transportation taxes—were the lead cause of drops in 13 cities.[10] These smaller sources also contributed to revenue drops in the remaining cities; combined, they were the second-leading factor of revenue performance in 14 localities.

In another five cities, declines in sales and income taxes—sources that tend to register economic shifts quickly—reduced collections. Property tax, an important income source for all 30 cities, led revenue decline in three Florida cities.

Intergovernmental aid triggered revenue declines in nearly one-third of the cities examined

Intergovernmental aid is an important revenue source for all 30 cities, but in nine—Baltimore, Boston, Cleveland, Houston, Las Vegas, Minneapolis, Philadelphia, Phoenix, and the District of Columbia—reductions in these receipts primarily drove falling revenue. (See Figure 4.) More than half of Cleveland's revenue decline, for example, was due to cuts in intergovernmental aid.

Further, in these cities, overall revenue declines were typically more severe than in those that relied less on aid from other governments. This is because heavy reliance on aid from other governments leaves cities vulnerable to the policy decisions and economic circumstances of those other governments and with fewer internal options for generating revenue. For instance, the American Recovery and Reinvestment Act contributed more than \$9.3 billion to the 30 cities.[11] Although these stimulus funds provided a short-term cash infusion that served as both a stopgap for cities' falling revenue and a jump-start for local economies, the recession's impact on state and local budgets continued longer than in the previous three recessions.[12] As a result, stimulus dollars ran out before many cities' own-source revenue recovered. Pew found that state aid to local governments began to decline in 2010, after the recession was officially over—a trend that continued through 2012.[13] As one-time stimulus dollars dwindle and new federal-level, budget-austerity measures make less money available for state and local governments, cities might not be able to rely on help from them to fill gaps resulting from their own still-shaky revenue.

FIGURE 4

Many Factors Contributed to Cities' Revenue Losses During and After the Great Recession

Primary causes of peak-to-trough revenue losses, by city

Lead Driver	*City*
Property Tax	Miami Orlando, FL Tampa, FL
Sales Tax	Atlanta Denver San Diego
Income Tax	Cincinnati New York
Other Taxes	Chicago Pittsburgh St. Louis
Intergovernmental Revenue	Baltimore Boston Cleveland Houston Las Vegas Minneapolis Philadelphia Phoenix Washington
Charges and Fees	Portland, OR
Nontax Revenue	Dallas Detroit Kansas City, MO Los Angeles Riverside, CA Sacramento, CA San Antonio San Francisco Seattle

Note: The following 20 cities studied collect a local sales tax: Atlanta, Chicago, Dallas, Denver, Houston, Kansas City, Los Angeles, Minneapolis, New York, Philadelphia, Phoenix, Pittsburgh, Riverside, Sacramento, San Antonio, San Diego, San Francisco, Seattle, St. Louis, and Washington.

The following 10 cities studied collect a local income tax: Baltimore, Cincinnati, Cleveland, Detroit, Kansas City, New York, Philadelphia, Pittsburgh, St. Louis, and Washington.

Nontax revenue includes revenue from investments primarily. It does not include intergovernmental revenue or charges and fees.

See the full methodology at pewstates.org/City-Fiscal-Methodology for more information on the distribution of city revenue sources.

What is intergovernmental aid?

Intergovernmental aid comprises grants, transfers, and other funds a city receives from federal, state, county, or other local governments. This category includes ongoing revenue-sharing agreements between governments and one-time infusions, such as federal funds from the American Recovery and Reinvestment Act of 2009 and the Federal Emergency Management Agency, or state grants for housing construction or infrastructure improvements. Consistent, detailed data on the amount of these federal awards were not readily available because cities do not report this revenue in the same way.

Although all states distribute aid to local governments, the amount varies among localities and among states. States also differ in how they provide aid to localities. Categorical aid provides funding with specific purposes and other restrictions. Unconditional aid supports local governments more broadly.

Declines in collection of other tax and nontax revenue had outsized effects

In many cities, officials are contemplating strategies to rely more on revenue sources they can directly control, particularly smaller ones such as charges and fees, business taxes, and income-generating investments.[14] These streams, however, typically represent lesser shares of total municipal revenue than intergovernmental aid, property taxes, and, in some cities, sales or income taxes. For purposes of this analysis, Pew aggregated these smaller revenue streams into "other tax" and "other nontax" categories and examined their impact on revenue losses. This research found that, between 2007 and 2011, declines in these streams played a larger-than-expected role in falling revenue across the 30 cities.

In 13 cities—Chicago; Dallas; Detroit; Kansas City, MO; Los Angeles; Pittsburgh; Portland; Riverside, CA; Sacramento; San Antonio; San Francisco; St. Louis; and Seattle—other tax and other nontax revenue were the leading causes of revenue decline:

- Other nontax revenue (mostly investment income) was the primary driver in **Dallas'** revenue fall from the peak in 2008 to the bottom in 2010.
- Similarly, **Kansas City's** losses in nontax revenue, specifically contributions and investment income, drove a $57 million loss in revenue between 2008 and 2010.[15]

- **San Antonio**, which owns the nation's largest municipally owned energy utility, presents another case in which nontax revenue was the primary factor triggering losses. The utility is a key element of the total revenue picture, and a decline of more than $33 million in receipts from 2008 to 2009 was a substantial reason for the city's slide from peak to trough.

Sales and income tax collections reacted quickly to changes in economic conditions

Cities differ greatly in how they rely on sales taxes. Among the cities studied, 20 levy a local sales tax, and 18 of those experienced declines in 2009, though the impact of the losses varied. (See Figure 5.) In cities such as Pittsburgh and Minneapolis, sales taxes account for less than 5 percent of total revenue, but in Phoenix and Houston, they are the second-largest source.

Income taxes are less common—levied in only 10 of the cities studied —but when imposed, they typically make up a large portion of municipal income, representing an average of 25 percent of total revenue. Like the sales tax, income taxes fell off quickly in reaction to the downturn. These collections dropped sharply in nine of the 10 cities in 2009.

Consumers' spending habits change quickly when the economy constricts and employment decreases. Similarly, income taxes dip immediately when unemployment rises and wages fall. Correspondingly, when economic conditions improve, these revenue sources improve swiftly, as they did in 2011. Revenue from sales and income taxes differs from property tax collections, which might not reflect economic shifts for several years.

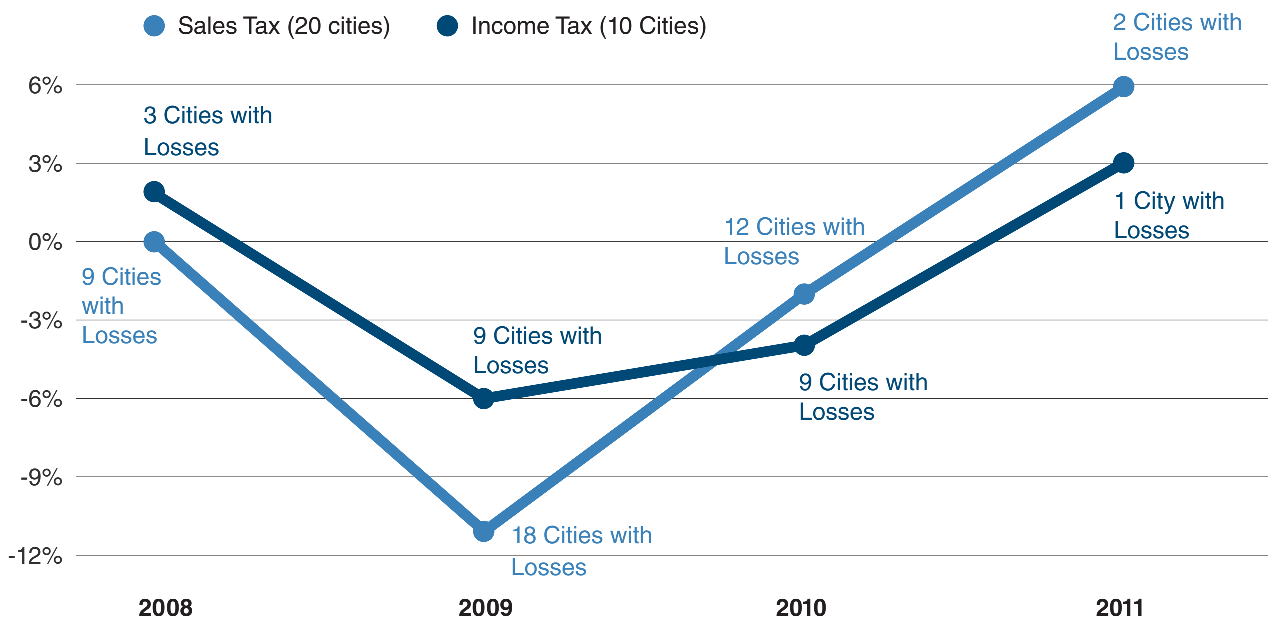
Losses in sales and income tax constituted the largest driver in total peak-to-trough losses for five cities—Atlanta, Cincinnati, Denver, New York, and San Diego.

- **Cincinnati** and **Cleveland** rely on income tax for the largest share of their total revenue. Income generated from the income tax decreased by $17 million and $24 million, respectively—a key cause in the total declines in both cities.
- In **New York**, the drop in sales taxes represented almost a quarter of the city's total revenue decline. By 2011, revenue had turned around and was growing—due in part to a rebound in sales tax collections.

FIGURE 5

Revenue Sources That React Quickly to Economic Changes: Change From Previous Year

Percent change in sales and income tax collections, by year



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The following 10 cities studied collect a local income tax: Baltimore, Cincinnati, Cleveland, Detroit, Kansas City, New York, Philadelphia, Pittsburgh, St. Louis, and Washington.

In response to declines in consumer spending during the Great Recession, several cities increased sales tax rates or taxes on consumption:

- In **Philadelphia**, a rate increase from 1 percent to 2 percent supported growth in sales tax collection.
- **Sacramento** passed by referendum a measure in November 2012 increasing the sales tax by 0.5 percentage points, with the intent to use the proceeds to restore some of the cuts to affected police and fire units.[16]
- **Los Angeles** (1 percent to 1.5 percent), **New York** (4 percent to 4.5 percent), and **the District of Columbia** (5.75 percent to 6 percent) also increased their rates in fiscal 2010.[17]

Property tax is the main driver for revenue loss in three Florida cities

The three Florida cities studied—Orlando, Miami, and Tampa—experienced deep revenue losses between 2007 and 2011, largely from declines in property tax collections. Property tax revenue fell in these cities in part because of changes in state law, enacted in 2007 before the recession and housing market crash, which imposed a 3 percent cap on assessment increases and required a one-time rollback to 2006 assessed values. Although these changes were intended to relieve tax burdens on new homebuyers in a booming market, they ultimately exacerbated declines in city property tax revenue.

How cities weathered revenue shortfalls

Cities rode out the Great Recession and its aftermath by employing a mix of financial management strategies and policy interventions. On the revenue side, cities raised taxes, gained aid from other governments, created new fees for services, and relied on property tax revenue, which, in most cities, did not reflect the impact of the housing crisis until 2010. City policymakers also cut spending and tapped reserves.

Property tax growth bolstered revenue during the Great Recession in many cities

The collapse of the housing market helped drive the country into a deep recession. But Pew found that property taxes, a major revenue source for nearly all 30 cities, softened the recession's blow in many cases by contributing to revenue growth or offsetting decline in real terms. In fact, collections were relatively strong, increasing in two-thirds of the cities between 2007 and 2011.[18] Much of the robustness of property tax as a revenue source over the five-year study period can be explained by its general lag behind market conditions. Some cities took additional steps to raise rates.

Strong property tax collections fueled a substantial portion of the total growth in the rebounding cities of Atlanta, Chicago, and Portland. In Atlanta, steps to raise property tax rates by $3.14 per $1,000 of valuation (36 percent) in 2009—the year in which city receipts hit bottom—led to substantial revenue increases over the next two years.[19] The additional $63 million in property taxes Atlanta collected between 2009 and 2011 accounts for nearly two-thirds of its revenue growth.

Beyond contributing to growth in rebounding cities, property taxes provided a bright spot for many still short of a full revenue recovery. Halfway through fiscal 2009, New York reversed a 7 percent property tax cut and eliminated a homeowner rebate program.[20] These changes contributed to $2.3 billion of property tax growth between 2009 and 2011, and boosted revenue close to the city's preceding high point.

Property taxes also offset declines. Among the cities examined, 18 experienced growth in property taxes even as total revenue was declining:[21]

- Despite the severe impact of the housing crisis in California, property tax collections in **San Diego** remained strong during the first few years of the study period. As other sources declined, pushing total city revenue from its peak in 2007 to a low point in 2010, these collections continued to grow by $41 million—easing the burden of shrinking sales taxes and other nontax income.
- In **Boston**, which has neither an income nor a sales tax and is highly dependent on a limited number of revenue streams, property tax collections increased $102 million between 2009 and 2011, as a result of a rate increase.[22] By 2011, the tax represented nearly $6 out of every $10 going into city coffers. Although these gains were substantial, they could not offset cuts in aid from other governments and could not save the city from a general downward trend to the revenue low point in 2011.[23] Nevertheless, Boston's recession would have been deeper if not for increased property tax receipts.

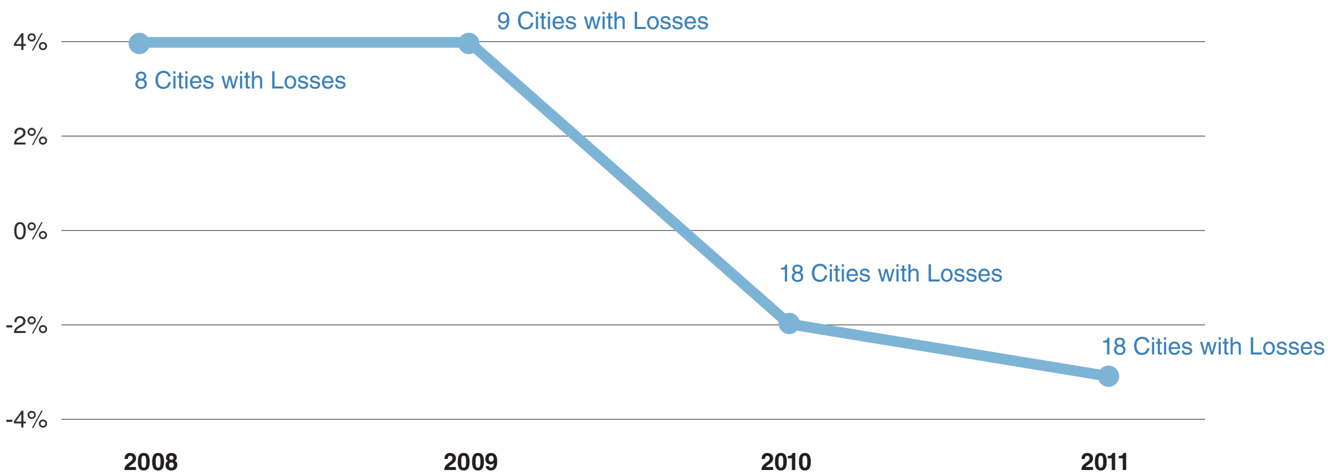
But, because of the lag between when property values declined and when some cities assessed those properties, many cities began to feel the effects of the housing crisis from lower property tax revenue in 2010 and 2011. Even when annual assessments were performed, there was often an 18- to 24-month gap in when properties were assessed and when taxes on that assessment were collected. In the district, property tax revenue in 2011 was based on 2009 assessed market values. Similarly, Miami's property tax rates were based on assessments conducted 15 months earlier, and so the city did not begin to see the effects of the depressed housing market until 2010 and 2011.

By the final two years of the study period, most of the 30 cities were experiencing declines in property taxes. (See Figure 6.) Twelve—Cleveland, Las Vegas, Los Angeles, Miami, Orlando, Riverside, Sacramento, San Antonio, San Diego, Seattle, Tampa, and the district—had decreases both years. Finally, in every city except four—Baltimore, Cleveland, Detroit, and Portland—taxable assessed values declined in 2011 from the year before, which added to the downward pressure on this key revenue source.[24] These trends indicate that, for many of these large cities, the impact of the housing crisis on local revenue could have just been starting, several years after the worst of the nationwide collapse.

FIGURE 6

Property Tax Collections Generally Did Not Begin to Decline Until Well After the Great Recession

Property tax year-over-year percent change by city, 2008-2011



Reserves were used to compensate for shortfalls

Revenue declines across the 30 cities forced hard choices for policymakers. Many programs for which cities are responsible represent basic elements of everyday life—public safety, trash collection, and street cleaning. Cuts to these services are felt immediately and can be disruptive, even harmful, to a city's long-term prospects, including its ability to attract and retain residents and businesses. To forestall or soften cuts in operational spending, every city with access to financial reserves—29 of the 30 studied—tapped those funds during the study period—often before implementing spending cuts.

Cities with reserve funds could lessen the impact of or stave off cuts and fill budget gaps.[25] Using reserves to address shortfalls can help avoid service reductions, but it is also a short-term solution that can compromise a city's long-term fiscal health:

- **Sacramento** tapped reserves consistently during and after the Great Recession, reducing fund balances from 31 percent of general revenue in 2007 to just 6 percent in 2011.[26] Although the city used its financial cushion to help close substantial shortfalls, it is now not as able to deal with future fiscal challenges.

- **Chicago** expended its reserves before 2007, and had very little financial cushion leading into the Great Recession. As the economic downturn hit, the city was forced to seek additional revenue from asset leases.
- **Denver** drew down $60 million in reserves in response to steep revenue declines in 2009. As fiscal troubles wore on, however, reserves could not fill the gap, and the city implemented spending cuts and a hiring freeze to help close the shortfall.[27]

Average reserve levels across the 30 cities declined from 18 percent of general fund revenue in 2007 to 14 percent in 2011. Budget pressures continued in 2011, and all cities faced the tough choice of setting aside money to prepare for the next downturn or using those dollars to address immediate spending pressures.

Cities cut spending, but preserved some core services

Squeezed revenue drove tough choices, and using reserve funds was not enough to close persistent budget gaps. Sacramento not only closed pools and community centers but also made cuts and layoffs to public safety, resulting in the elimination of the vice, narcotics, financial crimes, and undercover gang squads in 2011.[28] Police officers no longer responded to burglaries, misdemeanors, or minor traffic accidents as result of the reductions.

Regardless of the services for which each city is responsible, all 30 struggled to maintain the most essential ones during and after the downturn, and nearly all cut spending to deal with revenue shortfalls between 2007 and 2011.[29] Most of these cuts came after the Great Recession; 24 cities reduced operational spending between 2010 and 2011. Cuts came late for a range of reasons, including delayed revenue declines and tapping of reserves. As of 2011, in nearly half the cities examined, spending was below prerecession levels.

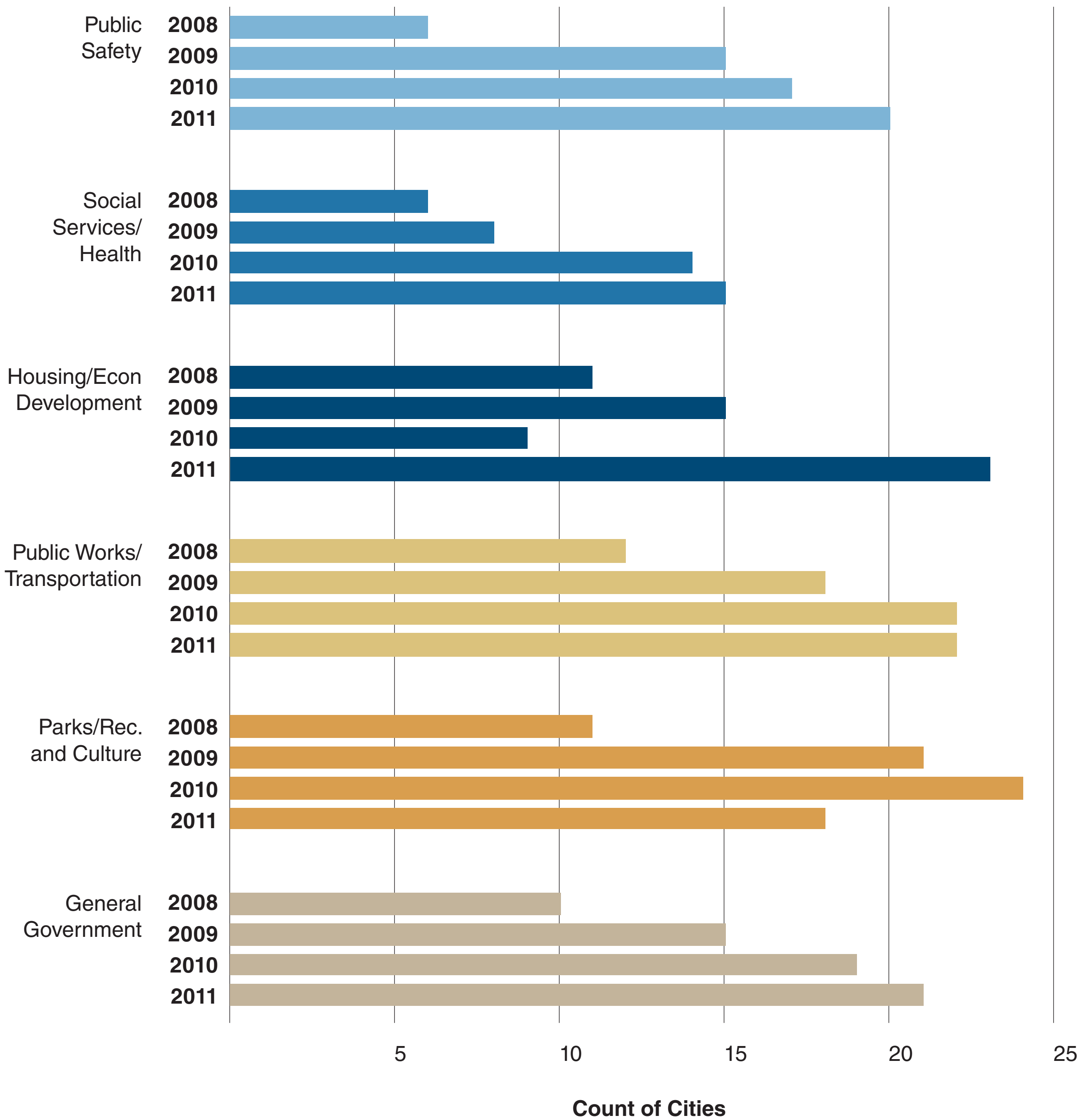
Most cities initially attempted to preserve public safety—for which all 30 are responsible and which both residents and government typically see as vital— by first cutting other budget areas and reducing municipal workforces. Between 2007 and 2009, more cities cut spending on housing and economic development, parks, recreation, and cultural facilities or public works and transportation than on public safety. (See Figure 7.) As revenue shortfalls persisted and reserves became depleted, cities turned to public safety, which represents the largest share of spending in nearly every city budget. By 2011, two-thirds of the cities were reducing public safety spending in real dollar terms.

In Dallas, for instance, revenue began to falter in 2009 and hit bottom in 2010. Heading into the downturn, the city made cuts to public works and transportation, with a $16 million, or 9 percent, reduction between 2008 and 2009. The city followed

FIGURE 7

Public Safety Was Typically the Last Budget Area to Face Significant Cuts

Year-over-year spending cuts: count of cities by category



Note: Only 20 of the 30 cities had spending classified as social and health services. They were: Baltimore, Boston, Chicago, Cincinnati, Cleveland, Dallas, Denver, Detroit, Houston, Kansas City, Las Vegas, Minneapolis, New York, Philadelphia, Phoenix, San Antonio, San Francisco, Seattle, St. Louis, and Washington. All cities except Chicago had spending classified as housing and economic development.

These counts reflect the number of cities cutting spending in real, inflation-adjusted dollars.

this with cuts to parks, recreation, and cultural facilities, first by $2 million in 2009, and then a notable $18 million—14 percent—in 2010. Although other spending areas were also cut, public safety, which dominates the city's budget, continued to grow from 2008 through 2010. In 2011, despite an infusion of intergovernmental aid and growth in own-source revenue, Dallas reduced total operating spending by 6 percent—achieved in large part by a $31 million cut to public safety spending.

Because of the recession, state and local governments across the United States reduced staff. All 30 cities cut their workforce, collectively eliminating nearly 40,000 positions between 2008 and 2011.[30]

- **Las Vegas** shed more than 600 positions, 270 of them through layoffs and the rest through attrition and a hiring freeze.[31]
- **Phoenix** cut over 2,500 jobs, leaving the city with its smallest per-capita workforce in 40 years.[32]
- **Chicago** cut the number of full-time equivalent positions in its budget by 8 percent.[33]

Reduced municipal payrolls translate to savings, but they also mean fewer workers to pave city streets, collect trash, police communities, and serve other vital functions. San Francisco reduced total operating spending by $15 million between 2009 and 2011, largely by cutting $38 million from social service and health activities, including a reduction of 327 full-time community health employees and 150 human welfare and neighborhood development employees.[34] Also, aid payments and assistance for human welfare and neighborhood development were reduced.[35]

Reducing the local workforce also means fewer public-sector jobs in the area's economy. If the gap is not made up through private-sector growth, these cuts could contribute to stubbornly high unemployment rates and lost revenue from income tax.[36]

The road ahead presents challenges

Even as the national economy recovers, substantial challenges remain for cities. Fiscal austerity at all levels of government will likely continue to affect municipal budgets. Although state revenue was rebounding by 2010, ongoing fiscal constraints suggest further contractions in federal and state aid to the nation's cities. Federal spending limits currently pose the most direct threat as states and city governments work to absorb the cuts.[37]

Further, in 2012 the national real estate collapse continued to reverberate as aggregate property tax revenue for all local governments in the country declined. Recent census data show small increases in total property taxes collected by all local governments in the first quarter of 2013, but these receipts, a foundation of municipal finance, will likely continue to be a concern.[38]

Beyond the current shaky revenue picture, some cities' long-term obligations threaten their near- and long-term finances; the annual cost of retirement benefits continues to rise, particularly in cities with severely underfunded pension and retiree health care obligations. As of fiscal 2010, the last fiscal year for which complete data are available, the 30 cities together faced more than $225 billion in unpaid commitments—$121 billion for pensions and $104 billion for retiree health care and other nonpension benefits. However, the size of the pensions funding gap varies considerably among cities. Among the cities in our study, only Washington had enough set aside to fully pay for its long-term promises, with a funding level of 111 percent.[39] Other cities, such as San Antonio, San Francisco, and Tampa, were close to fully funded, but half the cities ranged from 39 to 79 percent funded as of 2010. Not surprisingly, 25 of the 30 cities experienced a decline in funding levels between 2007 and 2010. For retiree health care and other benefits, half of the cities had not set any money aside to cover these liabilities as of 2010.

Further, in 2010, nearly half of the cities examined were not paying their full, recommended annual contributions to the funds meant to pay for these benefits, adding to the unpaid bill and putting off costs for future taxpayers to deal with. Deferring these obligations also means that future dollars available for the day-to-day operating functions and services on which citizens rely will be squeezed, as cities are forced to make up the difference for pensions and other post-retirement benefits.

The decline in reserves is also an issue. Although many cities had shored up their reserves by 2011, 18 of the 30 cities had slimmer reserve funds than in 2007, before the recession. These cities will face difficult choices between allocating dollars to immediate demands for services or rebuilding cushions to guard against future financial challenges.

Managing long-term obligations and setting aside money for a rainy day are critical components of cities' fiscal health, but they are only two factors. Each city will face other challenges in the near and long terms, and much will depend on revenue performance driven by economic activity, demand for services, and future investment decisions. (See Pew's city profiles at pewstates.org/City-Fiscal-Profiles for analysis on individual cities.)

Conclusion

Thirty of America's large cities faced persistent fiscal challenges from 2007 to 2011 and employed a variety of strategies to address them. These local governments raised taxes, drew down reserves, and ultimately cut spending when other measures were not enough. These steps, although needed to maintain financial stability, have long-term implications, such as reducing essential services, depleting rainy-day funds, and potentially diminishing cities' marketability to business and other investment, to name just a few. That more than two-thirds of these cities hit their revenue lows in 2010 or 2011 after the recession's end suggests that their fiscal challenges could continue in the years to come. Many will continue to deal with the aftermath of the nation's recent housing woes and a slow economic recovery. In addition, cuts in federal and state aid and greater demand for services portend a challenging road ahead for America's cities.

Appendix: Methodology

The primary data sources for this report are city Comprehensive Annual Financial Reports, or CAFRs, for fiscal 2007 through 2011. Pew researchers collected data from the statement of revenues and expenditures and the statistical section of each city's CAFR for every year in the study period. Although each city is unique, Pew organized revenue and expenditure line items into major groupings that are comparable across cities. To control for the effects of inflation, researchers adjusted dollar values reported in the CAFRs using the U.S. Bureau of Economic Analysis' National Income and Product Account estimates (a gross domestic product deflator).

Pew researchers then identified a "peak" and "trough" revenue year for each city. Peak years could occur at any point in the study period, while trough years were defined as the lowest revenue point between 2008 and 2011; this time frame specifically targets revenue declines caused by the Great Recession. Next, Pew grouped cities based on 2011 revenue performance relative to each city's prior peak to identify those experiencing a rebound—exceeding their previous revenue high points—and those still struggling to return to predownturn levels. Cities whose revenue remained below peak were further grouped based on whether revenue was still declining as of 2011 or was on an uptick somewhere between the city's previous low and high points.

For each city, Pew examined the primary drivers of revenue loss between peak and trough years, calculated the total revenue decline, and analyzed the share of that total loss represented by each individual revenue source. Similarly, for rebounding cities, Pew identified the revenue streams that were most responsible for financial gains between a city's trough year and the end of the study period. This strategy allowed researchers to assess trends across cities in the types of losses that drove revenue declines and the gains that spurred rebounds.

A more detailed discussion of the methodology is available at pewstates.org/City-Fiscal-Methodology.

Endnotes

1 Pew's adjustments facilitate comparisons across the 30 cities and over time, but it is important to note that each has a unique structure and oversees and operates different government functions. In addition, some local governments face greater constraints from county and state authorities in setting tax rates and raising new revenue; while others enjoy more autonomy. Cities' also differ in the range of services they provide. For example, four of the cities studied directly control and finance a school system, and others have different roles when it comes to building and maintaining infrastructure.

2 Pew calculations from the U.S. Conference of Mayors and the Council on Metro Economies and the New American City, *U.S. Metro Economies Outlook: Gross Metropolitan Product, and Critical Role of Transportation Infrastructure*, (2012), http://usmayors.org/metroeconomies/0712/FullReport.pdf.

U.S. Department of Commerce, Bureau of Economic Analysis, *National Income and Product Accounts—Gross Domestic Product, First Quarter 2013 (Third Estimate)*, (June 26, 2013), http://www.bea.gov/newsreleases/national/gdp/2013/pdf/gdp1q13_3rd.pdf.

3 Pew calculations from data in the U.S. Census Bureau's American Community Survey, 2011, http://www.census.gov/acs/www.

4 Although some cities raised taxes, others have limited options for bolstering falling revenue. Legislative and constitutional limits, imposed at both state and local levels, can dictate which taxes can be levied, the extent to which municipalities can raise rates, or the amount that can be collected through a tax.

5 State revenue reached its lowest point at the end of 2009, according to Pew's analysis. Notably, in Houston, 2011 revenue was slightly higher than in 2008. The city was on an upward trajectory, however, from 2007 to 2009. For purposes of this analysis, Pew researchers classified the 2011 low point as the city's "trough" year; discussion of the city's peak-to-trough decline refers to the change from 2009 to 2011.

6 Complete Comprehensive Annual Financial Report (CAFR) data for the 30 cities studied in this report was available only through fiscal 2011 at the time the analysis was conducted.

7 Another seven cities—Cleveland, Detroit, Kansas City, Las Vegas, Riverside, San Diego, and Seattle—experienced a small uptick but were still close to their low points in 2011.

8 These 16 cities are: Boston, Cleveland, Detroit, Houston, Kansas City, Las Vegas, Los Angeles, Miami, Minneapolis, Orlando, Phoenix, Riverside, Sacramento, San Diego, Seattle, and Tampa.

9 During the study period, The American Recovery and Reinvestment Act—also known as the stimulus—provided historic aid to state and local governments. Based on the cities' own financial reports, it is difficult to isolate how the amount and timing of stimulus funds provided directly to local governments influenced revenue performance as compared with aid from states.

10 In Dallas and San Antonio, the category of "other, nontax revenue" represents a substantial share of total city revenue, although in most cities these streams are relatively small shares.

11 Pew analysis of Recovery.gov, "Track the Money," self-reported grant data.

12 Tracy Gordon, *State and Local Budgets and the Great Recession*. The Russell Sage Foundation and the Stanford Center on Poverty and Inequality, (2012), http://www.stanford.edu/group/recessiontrends/cgi-bin/web/sites/all/themes/barron/pdf/StateBudgets_fact_sheet.pdf.

13 The Pew Charitable Trusts, *The Local Squeeze: Falling Revenues and Growing Demand for Services Challenge Cities, Counties, and School Districts*, June 2012, http://www.pewstates.org/uploadedFiles/PCS_Assets/2012/Pew_Cities_Local%20Squeeze_report.pdf.

14 Katherine Barrett and Richard Greene, "The Risks of Relying on User Fees," *Governing*, (April 2013), http://www.governing.com/columns/smart-mgmt/col-risks-of-raising-non-tax-revenue.html.

15 Other tax revenue includes levies on gas, hotels and restaurants, businesses, tobacco, and alcohol, among others. Pew combined smaller categories, along with revenue listed under "other" or "miscellaneous" and charges and fees in city CAFRs, into one "nontax revenue" category for purposes of this analysis. This "nontax revenue" includes contributions, investment and interest earnings, revenue from use of money or property, and cities' own "miscellaneous" or "other" categories. Charges and fees include licenses, permits, fines, and special assessments.

16 Ryan Lillis, "Sacramento Looks to Restore Budget Cuts After Passage of Sales Tax Hike," The Sacramento Bee (Nov. 8, 2012), http://www.sacbee.com/2012/11/08/4969193/sacramento-looks-to-restore-budget.html.

17 California State Board of Equalization, *California City and County Sales and Use Tax Rates*, Publication 71, (2013.), p. 13, http://www.boe.ca.gov/pdf/pub71.pdf; New York State Department of Taxation and Finance, *Enactment and Effective Dates of Sales and Use Tax Rates*" (2012), http://www.tax.ny.gov/pdf/publications/sales/pub718a.pdf; District of Columbia, *Comprehensive Annual Financial Report, Year Ended September 30, 2011*, p. 171.

18 According to Pew's analysis, property taxes were the only own-source revenue category with median growth across the 30 cities between 2007 and 2011.

19 Property tax rates increased from $8.80 per $1,000 of valuation in 2009 to $11.94 a year later. City of Atlanta, *Comprehensive Annual Financial Report, for the Year Ended June 30, 2011* (2012) p. 149.

20 Thomas P. DiNapoli and Kenneth B. Bleiwas, Office of the State Comptroller and Office of the State Deputy Comptroller for the City of New York, *Review of the Financial Plan of the City of New York*, (December 2012), pp. 28-29, http://www.osc.state.ny.us/osdc/rpt7-2010.pdf.

21 Atlanta, Baltimore, Boston, Chicago, Cincinnati, Dallas, Kansas City, Las Vegas, Los Angeles, New York, Phoenix, Portland, San Antonio, San Diego, San Francisco, Seattle, St. Louis, and the District of Columbia.

22 Part of the reason property tax collections are such a large piece of total revenue in Boston is that the city is one of four examined that operates and funds its school system. As a result, the city collects school districts' property tax levies that in many jurisdictions go to independent school boards. City of Boston, *Comprehensive Annual Financial Report, for the Fiscal Year Ended June 30, 2012*, (2012.), p.68.

23 The weighted average of residential, commercial, and industrial levies increased from $16.63 per $1,000 of property value in 2009 to $19.15 in 2011. Residential rates grew 20 percent, from $10.63 to $12.79, and commercial, industrial, and personal property tax rates increased 14 percent, from $27.11 to $31.04 per $1,000.

24 Data for taxable assessed property values come from the 29 city CAFRs, but Chicago's 2011 CAFR does not include the data for the most recent year. Its 2011 figure instead came directly from the City of Chicago.

Chris Nash, Assistant Budget Director, pers. comm., March 15, 2013.

25 New York State mandates that the city carry no reserves. The state continues to play a key role in the financial oversight of New York City. Scheduled to terminate on July 1, 2008, the Financial Emergency Act was effectively extended until 2033. Though the law no longer gives the state control of the city's budget, it still reviews and monitors financial plans, major budget and policy issues, and other economic decisions. New York State, Office of the State Comptroller, *New York City Fiscal Oversight*, http://www.osc.state.ny.us/osdc/index.htm. As a result of the city's lack of a financial cushion, it borrowed from assets set aside for retiree health care obligations to close budget gaps; see DiNapoli and Bleiwas, *Review of the Financial Plan of the City of New York*, p. 25.

26 This report measures each city's unreserved general fund balance as the sum of the "assigned" and "unassigned" portions as defined by the Governmental Accounting Standards Board, or GASB, Statement No. 54 and as the "unreserved" portion as defined by GASB prior to Statement No. 54 going into effect. See the full methodology at pewstates.org/City-Fiscal-Methodology for a detailed explanation. The General Fund Economic Uncertainty Reserve goal is to maintain 10 percent of general fund revenue; as of 2012 the level was 4 percent. City of Sacramento, *Proposed Budget, Fiscal Year 2011/2012*,. p. 20, http://www.cityofsacramento.org/finance/budget/documents/FY12ProposedBudget-Web.pdf.

27 Lucy McFadden, . "Hick: Gird for cuts, Denver," *The Colorado Statesman*, July 17, 2009, http://www.coloradostatesman.com/content/991152-hick-gird-cuts-denver.

28 Erica Goode, "Crime Increases in Sacramento After Deep Cuts to Police Force," The New York Times, November 3, 2012, http://www.nytimes.com/2012/11/04/us/after-deep-police-cuts-sacramento-sees-rise-in-crime.html?pagewanted=all&_r=0.

29 Every city except New York reduced operational spending at some point between 2007 and 2011. New York held spending constant twice over the period, and increased it less than .5 percent in 2009 and 2011.

30 Pew calculation based on city CAFR data for full-time-equivalents, or FTEs. Data for local governments as a whole indicate employment continued to grow through August 2008; Lucy Dadayan and Donald J. Boyd, *The Depth and Length of Cuts in State-Local Government Employment Is Unprecedented* (Issue Brief), The Nelson A. Rockefeller Institute of Government, State University of New York, Albany (2013), http://www.rockinst.org/pdf/government_finance/2013-01-09-State-Local_Government_Employment.pdf.

31 Alan Choate, "Las Vegas Fiscal Year Spending Approved," *Las Vegas Review-Journal*, May 17, 2011, http://www.reviewjournal.com/news/government/las-vegas-fiscal-year-spending-approved.

32 City of Phoenix website, "Employee Count Per Capita Smallest in 40 Years Even as City Continues to Grow,"(2010), http://phoenix.gov/news/110410employees.html.

33 City of Chicago, Illinois,. *Comprehensive Annual Financial Report, for the Year Ended December 31, 2010* (2010), p. 170.

34 City and County of San Francisco, California, *Comprehensive Annual Financial Report Year Ended June 30, 2011*, (2011), p. 221.

35 Ibid., p. 12.

36 Nicholas Johnson, "The State and Local Drag on the Recovery," *Off the Charts: Policy Insight Beyond the Numbers*, Center on Budget and Policy Priorities website, June 8, 2012, http://www.offthechartsblog.org/the-state-and-local-drag-on-the-recovery.

37 Sequestration is not just a one-year event. It is $85 billion in automatic cuts for 2013 but also includes a $109 billion annual reduction in appropriations from 2014 through 2021. As the fiscal 2014 appropriations process moves forward, there could be bigger cuts than sequestration looming—especially if Congress addresses the cost of Medicaid with additional cuts. Note that these statements refer to total operational spending and do not account for small reductions that were offset by larger increases in other areas at the same time; Dylan Matthews, "The Sequester: Absolutely Everything You Could Possibly Need to Know, in One FAQ." *Washington Post*, Feb. 20, 2013, http://www.washingtonpost.com/blogs/wonkblog/wp/2013/02/20/the-sequester-absolutely-everything-you-could-possibly-need-to-know-in-one-faq.

38 Lucy Dadayan and Donald J. Boyd, *Strong Gains in the First Quarter; Mounting Uncertainty for the Rest of 2013*, State Revenue Report No. 92 (August 2013), The Nelson A. Rockefeller Institute of Government, http://www.rockinst.org/newsroom/revenue_reports/2013/2013-08-08-SRR_92.pdf.

39 The funding level for the District of Columbia represents only liabilities accrued since 1997 in defined benefit pension plans for firefighters, police, and teachers. In 1997, the federal government took over financial responsibility for benefits accrued by those workers up to then, as well as retirement benefits for judges, relieving the city of $4.9 billion in unfunded liabilities that it had inherited from the federal government. The city also contributes to a defined benefit plan (for 2,700 general municipal workers hired before 1987) that is managed by the federal Civil Service Retirement System, but an estimate of the city's share of those liabilities could not be obtained. This study does not include the costs of pension benefits for general municipal employees hired since October 1987. They are not in a defined benefit pension plan but instead receive benefits through a defined contribution system in which the city deposits money each year into a retirement account for each employee. See Government of the District of Columbia, *Comprehensive Annual Financial Report 2011* (Sept. 30, 2011), 111-117, http://cfo.dc.gov/sites/default/files/dc/sites/ocfo/publication/attachments/ocfo_cafr_2011_r.pdf.

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