

# Impact of Economic Crisis on Local Government

Tennessee Advisory Commission on  
Intergovernmental Relations

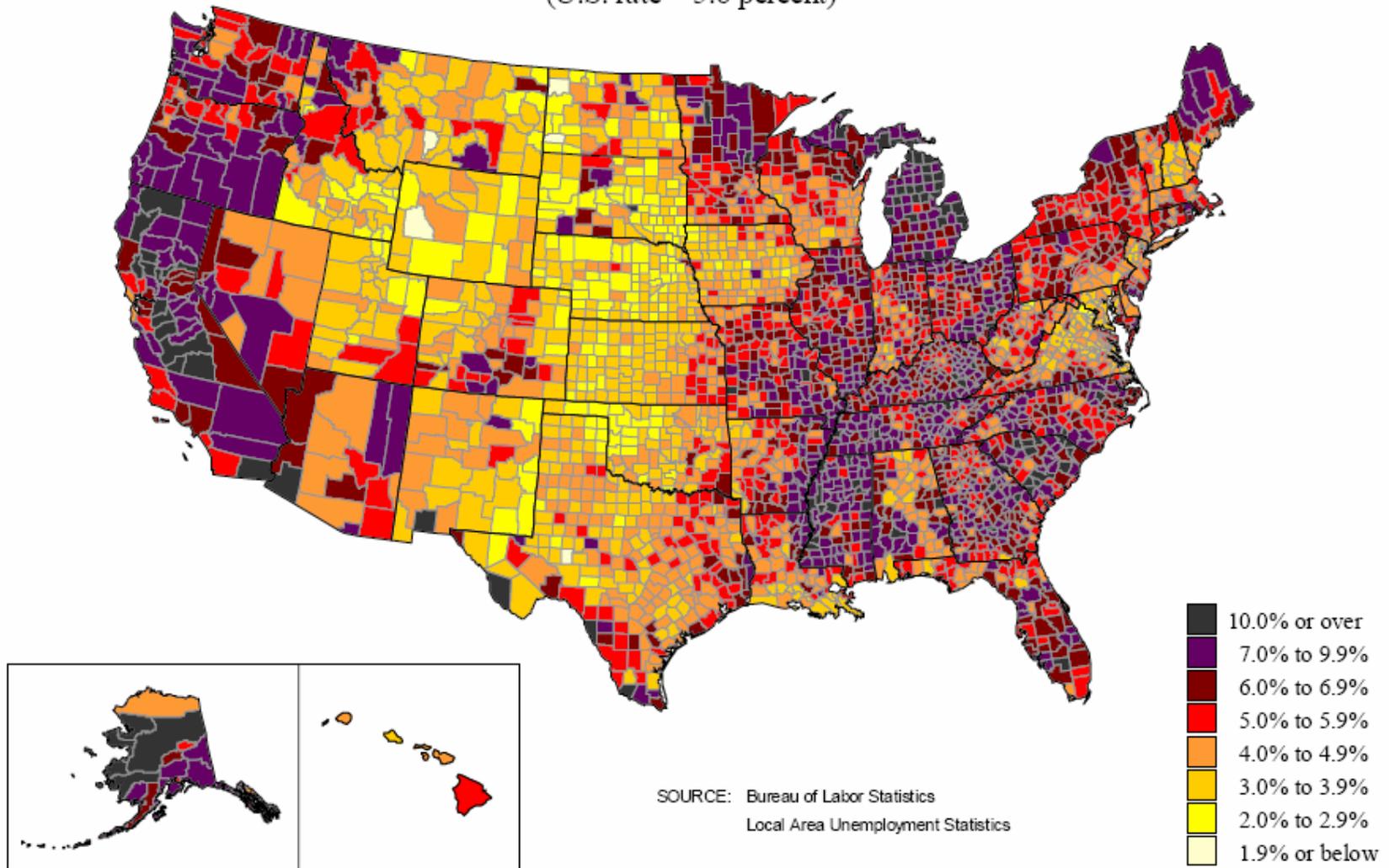
January 27, 2009

# Primary Revenue Sources for County Government

- Sales Tax
  - Property Tax
  - Petroleum Taxes
- Sales Tax Revenues for both state and local governments are adversely impacted by any economic slow-down. Fluctuations are expected.
  - This particular crisis has had elements that specifically affect both property tax and gas tax revenues.

# Unemployment rates by county, December 2007 - November 2008 averages

(U.S. rate = 5.6 percent)



# Differences Between State and Local Tax Base

- State Government – Sales Tax and Franchise and Excise Taxes
- Local Government – Sales Tax and Property Taxes
- Variations in State and Local Sales Tax Base

# Volatility of Local Sales Tax Base

- The sales tax base may vary greatly from one county to another.
- Generally, the larger the retail activity in a county, the greater potential for volatility.
- If a county has a relatively stable sales tax base, it is probably limited.
- A single store opening or closing can impact a small county.
- Walmart effect – other retailers show loss, they show gain.
- Single article cap

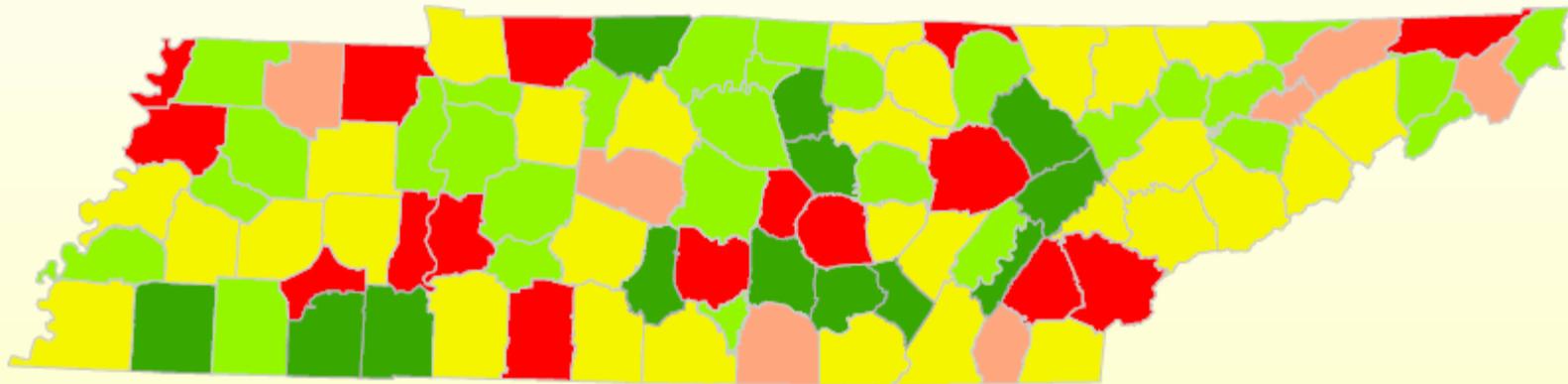
# Single Article Cap

- ⦿ State rate of 7% on full purchase price.
- ⦿ Local option sales tax (up to 2.75%) only applies to the first \$1600 of the purchase price of a single article.
- ⦿ Additional state rate of 2.75% applies on value from \$1600 to \$3200.
- ⦿ \$1600 purchase generates a maximum of \$44 in local option sales tax.
- ⦿ Likewise, a \$16,000 purchase also generates a maximum of \$44 in local option sales tax.

# Performance of Local Option Sales Taxes

- Some communities were experiencing reductions in sales taxes revenue last fiscal year.
- Others were able to fend off losses due to rate increases or the opening of large new retail facilities.
- The creation of new retail facilities may result in migration of revenue rather than generation of additional revenue.

FY 2007 to FY 2008  
Increase/Loss Percentage of Sales Tax Revenues

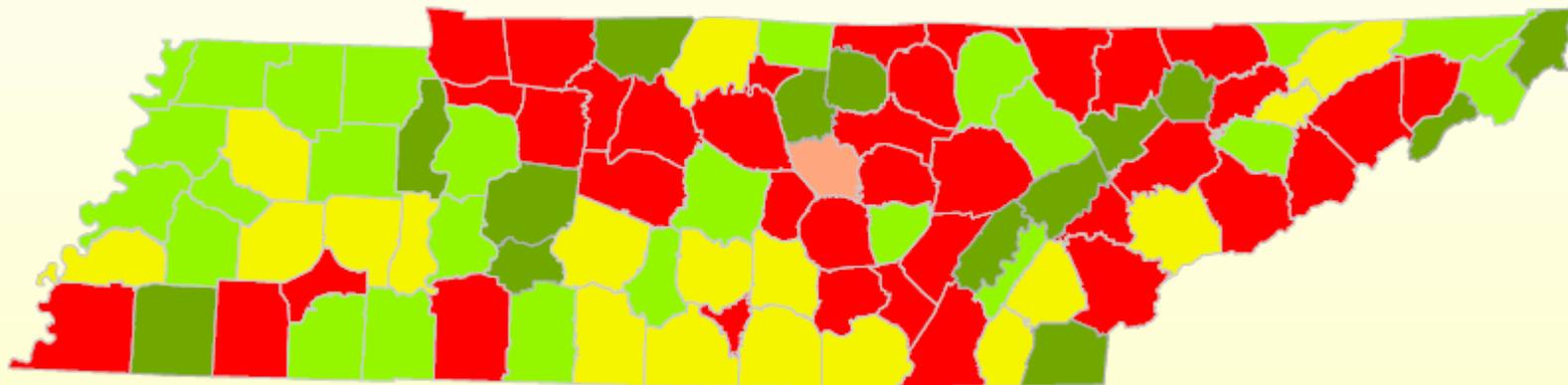


Statewide average: Increase of 1.8 %

**Percent Gain or Loss**

- Greater than 0.5 percent loss
- Up to 0.5 percent loss
- 0.1 - 2.5 Gain
- 2.6 - 7.5 Gain
- Greater than 7.5 gain

July - Sept 07 vs. July - Sept 08  
Increase/Loss Percentage of Sales Tax Revenues

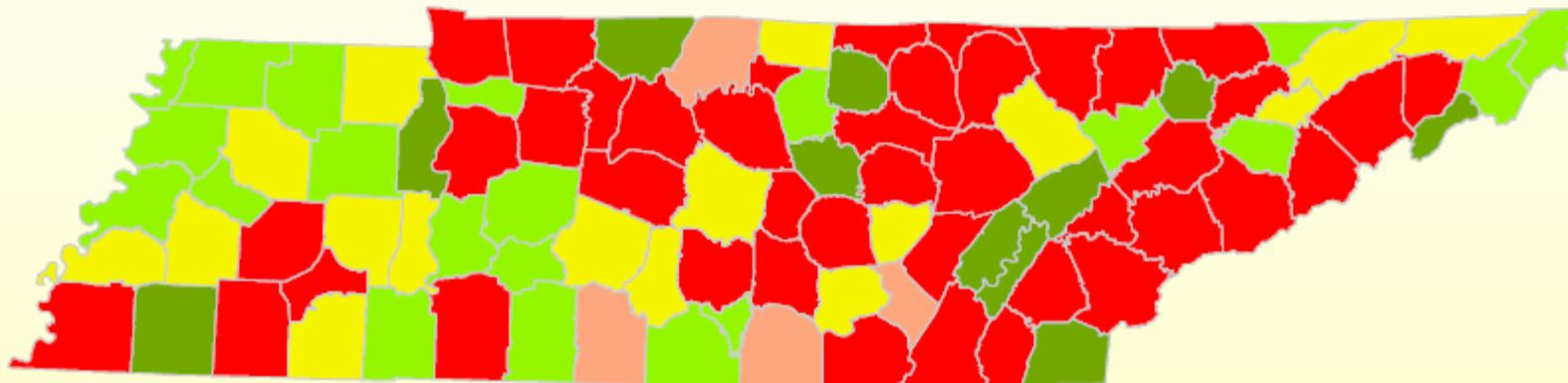


Statewide average: Increase of 0.6 %

**Percent Gain or Loss**

- Greater than 0.5 percent loss
- Up to 0.5 percent loss
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July - Dec 07 vs. July-Dec 08  
Increase/Loss Percentage of Sales Tax Revenues

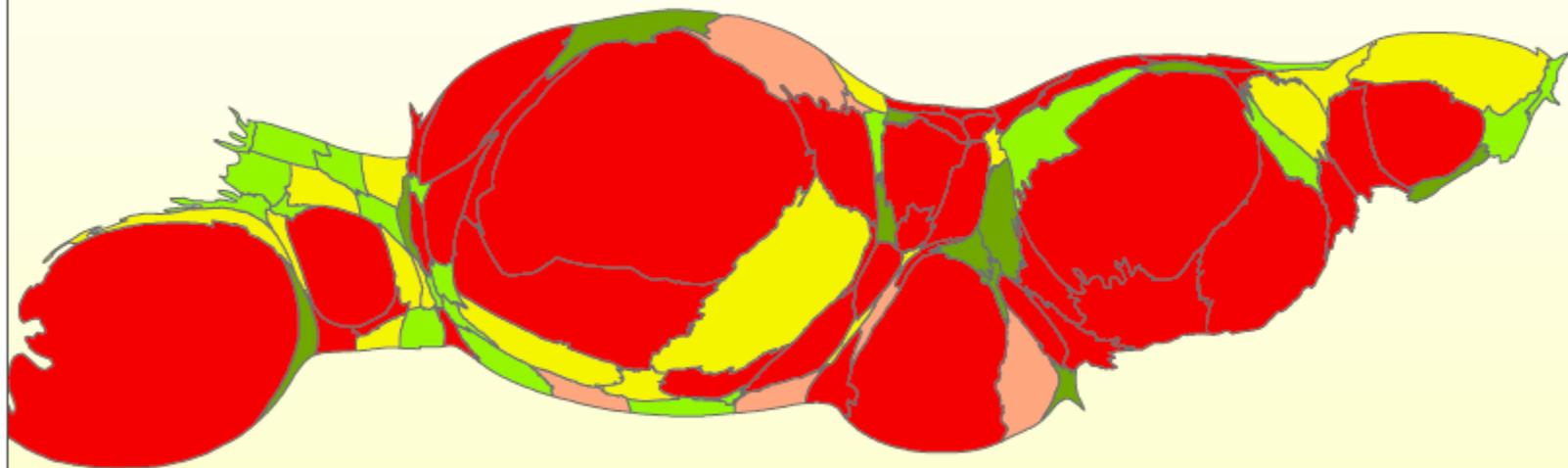


Statewide average: Loss of 1.4 %

**Percent Gain or Loss**

- Greater than 0.5 percent loss
- Up to 0.5 percent loss
- 0.1 - 2.5 Gain
- 2.6 - 7.5 Gain
- Greater than 7.5 gain

July - Dec 07 vs. July-Dec 08  
Increase/Loss Percentage of Sales Tax Revenues  
County Size In Proportion to FY 08 Revenue Dollars



Statewide average: Loss of 1.4 %

**Percent Gain or Loss**

- Greater than 0.5 percent loss
- Up to 0.5 percent loss
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# Impact of Reduced Sales Tax Collections

- Reduced Sales Tax Collections Particularly Hit Education Funding
- Counties will use fund balance to make up for shortfalls
- Maintenance of Effort provisions require a local funding body to set up a reserve account and make up for revenue shortfalls
- Revenue in some cases is pledged to bonded indebtedness
- Results in property tax increases.
- Loss of big ticket sales will become more apparent in local business tax collections in the Spring.

# Impact of Economic Crisis on Housing and Property Taxes

- ⊙ Reduction in home values or slow-down in growth of residential property values.
- ⊙ Impact will be felt over time as re-appraisals occur.
- ⊙ Increase in foreclosures.
  - Affect property tax collections and home values through “collateral damage”
- ⊙ Increase in appeals of assessment valuation.
- ⊙ Increase in cost of collections.
- ⊙ Loss of manufacturing facilities
- ⊙ Reduction of business inventory and equipment and resulting business personal property taxes.

# Petroleum Taxes

- July - December collections for 2008 show a 5.9% reduction from collections for the same period in 2007.
- Growth in gas tax revenues has been flat for years.
- Now showing actual decline as road miles driven declines
- Also impacted by changes in buying habits as consumers respond to gas prices.
- As popularity of smaller, more fuel efficient vehicles rises, consumer consumption is reduced.
- Per gallon tax structure results in revenue losses when gas prices spike.

# Petroleum Costs

## The Other Side of the Coin

- ◎ Bituminous Index (Cost of a Ton of Asphalt)
- ◎ January 2000 - \$150
- ◎ January 2008 - \$306.54
- ◎ July 2008 - \$604.62
- ◎ Sept. 2008 - peaked at \$742.31
- ◎ Costs of asphalt during much of the peak paving season in 2008 were double the costs paid in 2007.
- ◎ Other construction costs (steel, rock, fuel, etc.) are also highly inflated.
- ◎ Repairs and maintenance are postponed.
- ◎ Mineral Severance collections go down.
- ◎ County Highway departments are already planning layoffs.

# Business Tax and Bank Excise

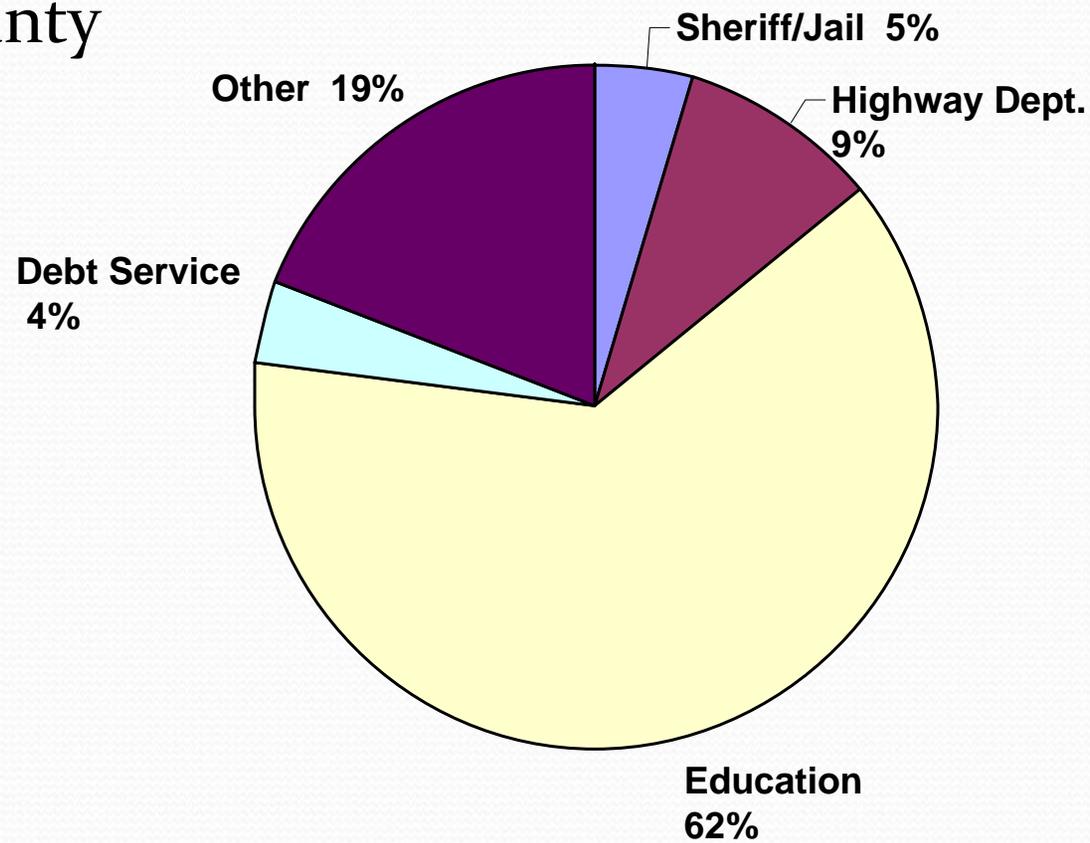
- ⦿ These would be the local taxes comparable to state franchise and excise taxes.
- ⦿ Loss in car sales will show up in lost local business tax collections. (June 1)
- ⦿ Lumber and building materials. (Mar 1)
- ⦿ Losses in the stock market should also depress Hall Income Tax collections.
- ⦿ Bank excise taxes are also expected to be down.

# Mandatory Spending

- ⦿ K-12 Education funding has a maintenance of effort requirement.
- ⦿ Local funding for highway departments must be maintained at a 5 year average or state revenues are lost.
- ⦿ Personnel expenditures in the Sheriff's department cannot be reduced without the Sheriff's consent
- ⦿ Other elected and appointed officials may bring "salary suits" for staffing and personnel needs and compel expenditures.
- ⦿ This leaves little room for cuts.

# Profile of Median County Budget

Giles County



# Property Tax Rate Increases

2008-2009	26 counties
2007-2008	34 counties
2006-2007	20 counties
2005-2006	24 counties
2004-2005	37 counties
2003-2004	37 counties
Total	178 increases

# Conclusions

- ◎ Like the state, local governments are experiencing reductions in sales tax revenue.
- ◎ Losses in property tax collections will be experienced later in the year and over time through re-appraisals.
- ◎ Counties will also experience budgetary hits as Business taxes, Hall Income Taxes and Bank Excise Taxes are paid later in the fiscal year.
- ◎ Petroleum tax losses combined with inflationary costs in transportation and highway maintenance are the most urgent need.