Executive Summary

While states slowly recover in the wake of the Great Recession, local governments have been hit with a one-two punch: State aid and property taxes, which together account for more than half of local revenues, are dropping simultaneously for the first time since 1980. The blow comes as demand for government services rises, driven by stubborn unemployment rates, population growth, and other factors.

State aid funds nearly a third of local government budgets on average. It fell by $12.6 billion, or 2.6 percent, in fiscal year 2010, the most recent year for which comparative data are available.[1] This trend has continued, with 26 states reporting cuts for fiscal year 2011 and 18 doing so thus far for 2012.[2] Some cities, counties, and school districts are fighting back with lawsuits. Before 2010, state funding was covering a smaller share of localities' growing expenses, falling from 33 percent in 2000 to 30 percent in 2009.

Property taxes, which amount to 29 percent of local government revenues, also are shrinking, reflecting the drop in real estate prices during the recession. In 2010, property tax revenues were $11.9 billion, or 2.5 percent, lower than the year before, the first annual decline since the mid-1990s and the largest in decades. They fell again in 2011, by another 3.1 percent, or $14.6 billion, and are expected to decrease further in 2012 and 2013.[3] This is different from past economic downturns, when home values and property tax revenues remained relatively stable.

DIVING DEEPER: THE AMERICAN CITIES PROJECT

Like all local governments, the nation's largest cities are facing heightened fiscal stress and often have to do more with less to meet residents' needs. In the coming months, Pew's American Cities Project will explore how economic trends, demographic shifts, and changes in service delivery are affecting 30 major cities. The project will help policy makers understand shared challenges and promising approaches.

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Some localities have raised taxes and fees to try to generate more revenues. But most have tackled budget pressures by reducing spending. Policy makers have increased class sizes and shortened school days; cut a wide range of services, from public safety to trash collection; and privatized or consolidated certain functions, such as maintaining parks and handling 911 calls. They also have eliminated public sector jobs, shedding half a million employees, or more than 3 percent of the local government workforce, since September 2008 through layoffs and attrition. Half of those were teachers and other school administrators or staff members.[4]

The local squeeze will be felt for years to come. The nation's ongoing housing crisis and fragile economic recovery, the likelihood of additional cuts in federal and state aid, and greater demand for services all presage a rough road ahead for local governments.