THE STATE OF COUNTY FINANCES
PROGRESS THROUGH ADVERSITY

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NACo TRENDS ANALYSIS PAPER SERIES, ISSUE 6 • OCTOBER 2016 • www.NACo.org

County governments provide essential services to create healthy, safe, vibrant and economically resilient communities. The Great Recession and the slow recovery affected both the county economies and the fiscal conditions of county governments.[1] Building upon the foundation laid by NACo's *Counting Money* study on county financial reporting, this analysis examines trends in annual county revenues and expenses between 2007 and 2013, the latest year available for the majority of audited county financial statements.[2] Using the fiscal data from the largest group of county governments reporting their financials in the same format (2,112 counties in 45 states and the District of Columbia), this report sheds light on the effect of the recession on counties and provides direction on the fiscal recovery of county governments.[3] The evidence suggests:

GENERAL REVENUES **DID NOT RECOVER** TO 2007 LEVELS IN **NEARLY HALF OF COUNTIES** BY 2013.

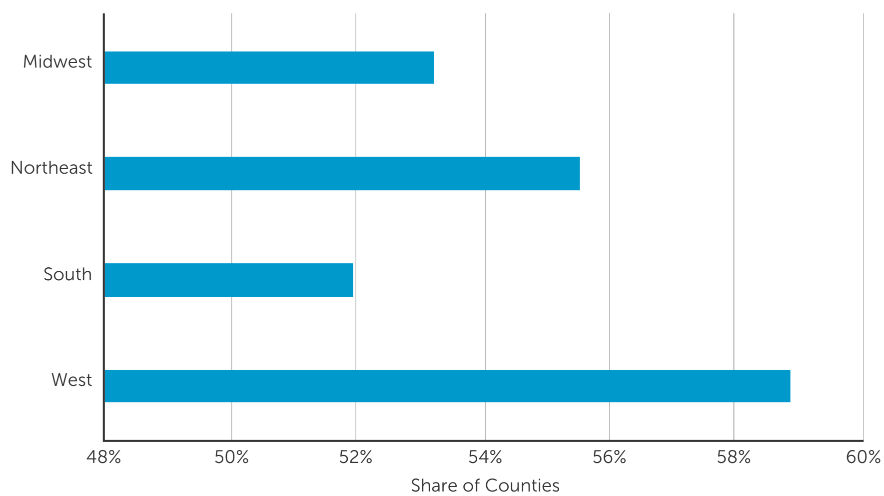
1 GENERAL REVENUE RECOVERY HAS BEEN SLOW AND UNEVEN ACROSS COUNTIES.

General revenues did not recover to 2007 levels in nearly half of counties (46 percent) by 2013, taking into account inflation. General revenues are discretionary funding, providing county boards the flexibility for allocating funds to needed services. This source of funding is primarily derived from taxes, fees and fines and any grants not restricted to a particular activity.[4]

The recovery has been uneven across counties. Overall, Western region counties recorded the most improvement through 2013, with 59 percent bouncing back to pre-recession levels (Figure 1). Backed by economies benefiting from rising oil and gas production between 2007 and 2013, the majority of counties in states such as North Dakota, South Dakota and Texas recorded higher general revenues in 2013

FIGURE 1: THE RECOVERY HAS BEEN UNEVEN ACROSS COUNTIES

Share of Counties with 2013 General Revenues Above 2007 Level, Inflation-Adjusted



Source: NACo analysis of data from the statement of activities in 2007 and 2013 audited county financial statements

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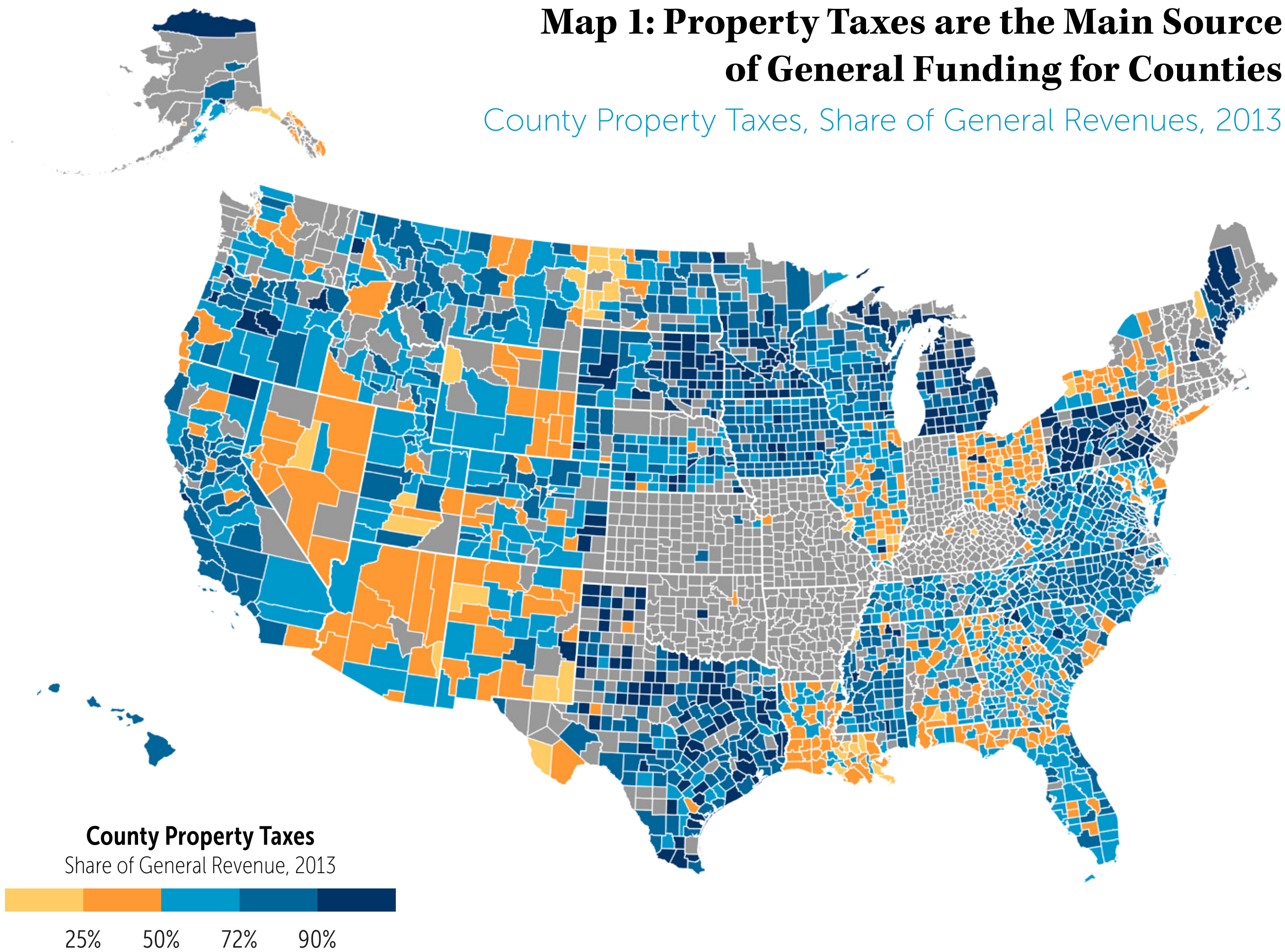
72% OF COUNTY GENERAL **REVENUES** ARE GENERATED BY **PROPERTY TAXES**.

compared to six years before. In contrast, Southern counties were still reeling from the effects of the recession in 2013, with almost half of them below 2007 levels. Large counties (those with populations higher than 500,000) were affected the most, with more than two thirds not yet at pre-recession levels.

Map 1: Property Taxes are the Main Source of General Funding for Counties

County Property Taxes, Share of General Revenues, 2013



Note: The counties marked in grey fit into one of the following categories: do not have county governments, do not report their financials with basic financial statements or their statements of activities for 2007 and/or 2013 were not available. For more on the methodology, see the Methodological Appendix and the report Counting Money: State and GASB Standards for County Financial Reporting.

Source: NACo analysis of data from the statement of activities from the 2007 and 2013 audited county financial statements

Property tax revenues drove the performance of county general funding. In 2013, property taxes comprised 72 percent of county general revenues (Map 1).[5] Property tax collections lag price movements in the real estate market because of the variety of assessment cycles around the country.[6] For example, South Carolina requires counties to conduct a reassessment every five years, while Michigan mandates annual assessments.[7] As a result, real estate market peaks precede peaks in property assessments and tax collections, sometimes by several years. The timing of the property assessment may mitigate or magnify the negative impact of real estate price decline on property tax collections. At the same time, rapid real estate price increases do not fully translate into increases in county property tax revenues due to various state limits on property tax increases.[8] Forty-one (41) states had at least one type of limitation on county capacity to raise property taxes.

The recession and slow recovery suppressed consumer spending and sales tax revenues. Two-thirds of counties that collected sales taxes in 2007 saw their revenues from this source of funding decline by 2013. Not all states allow counties to collect sales taxes: of the 29 states granting counties this authority, counties in 19 states won voter approval to introduce local sales taxes. For example, in many Louisiana parishes and counties in New York and Ohio, sales and use taxes represented about 26 to 48 percent of county general revenues in 2013.

65% OF **COUNTIES** COLLECTING **SALES TAXES** RECORDED **DECLINES** IN THIS **REVENUE SOURCE** BETWEEN 2007 AND 2013.

2 COUNTIES ARE STRUGGLING WITH RISING COSTS OF MANDATED SERVICES.

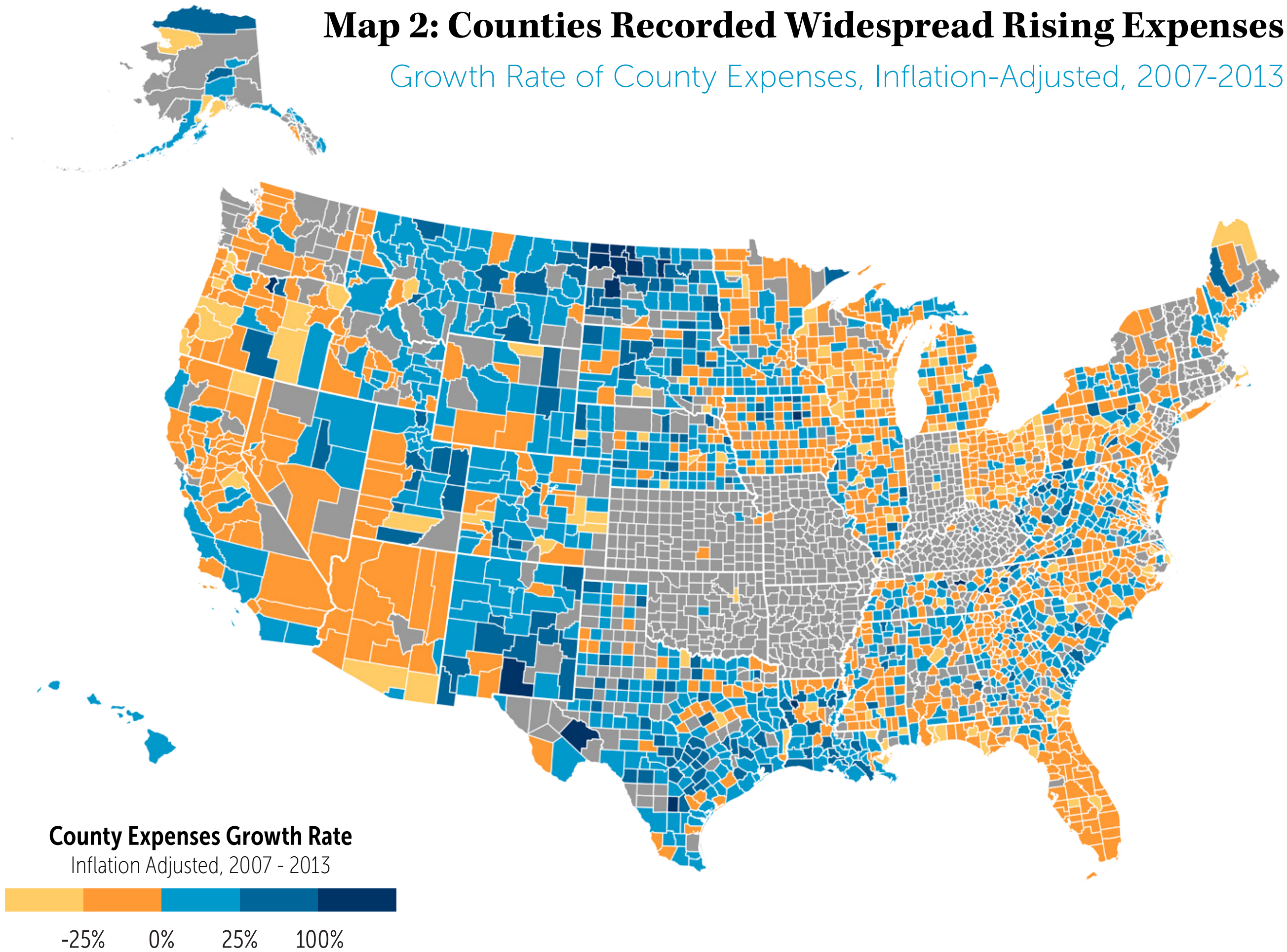
For governments, economic downturns translate into less revenue and higher volumes of services, as they try to deal with unemployment, business closures and more people in need. This fiscal squeeze is even more pronounced for county governments, being primary social safety net providers on the ground. With the economic recovery slow to take hold across counties, county governments struggle to meet state and federal mandates while serving their residents at adequate levels.[9]

Nearly half of counties (48 percent) recorded overall 2013 expenses above their 2007 levels, even when adjusted for inflation (Map 2).[10] Over one fifth of parishes in Louisiana and counties in North Dakota, Utah and West Virginia experienced expense increases of more than 30 percent. Pressure increased on small counties (those with less than 50,000 residents), with about 55 percent registering expense increases. In some counties, expenses more than quadrupled in six years (in Dunn County, ND and Mountrail County, ND). At the core of the recession, large counties (those with populations higher than 500,000) were more likely to record lower expenses. Only 35 percent recorded expenses rising over the six-year period analyzed.

48% OF **COUNTIES RECORDED** OVERALL 2013 **EXPENSES ABOVE** THEIR 2007 LEVELS.

Map 2: Counties Recorded Widespread Rising Expenses

Growth Rate of County Expenses, Inflation-Adjusted, 2007-2013



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Source: NACo analysis of data from the statement of activities in 2007 and 2013 audited county financial statements

Many mandated services saw widespread cost increases.

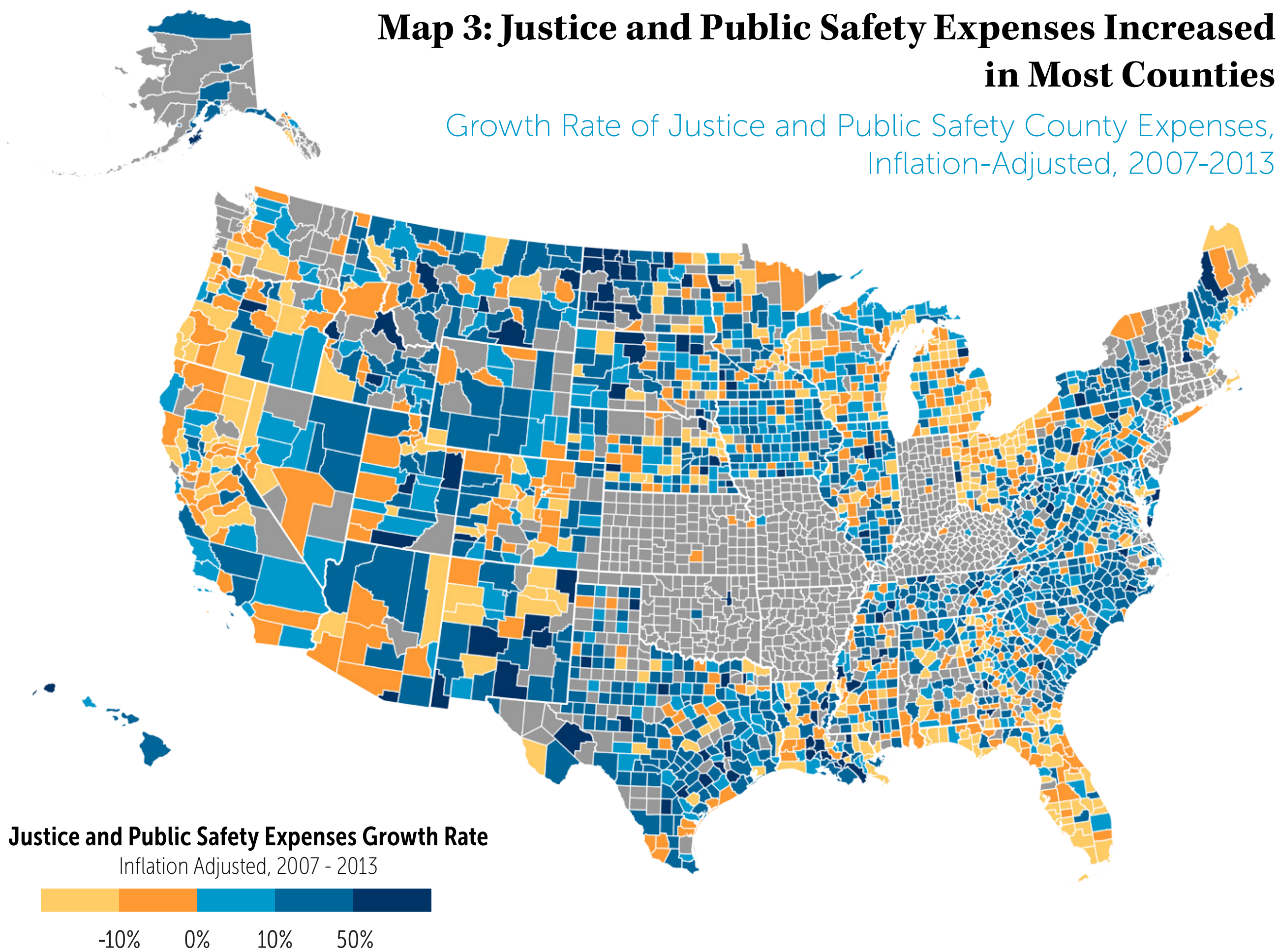
Justice and public safety county costs rose across the country. Two thirds of counties (65 percent) witnessed increases in justice and public safety expenses between 2007 and 2013, above the overall rise in prices (Map 3).[11] In many cases, justice and public safety expenses were the top cause of the increase in overall expenses. Alaska boroughs and counties in North Dakota and West Virginia had the highest surges of justice and public safety costs between 2007 and 2013. Counties are the first respondents in case of disaster: they operate 911 centers, run the sheriff departments and the county courts and operate and maintain county jails. Justice and public safety costs vary widely among counties, but typically account for 27 percent of county expenses. For more than a fifth of Georgia and Texas counties and over 80 percent of Maine counties, justice and public safety is a majority of county expenses.

65%

OF COUNTIES WITNESSED **INCREASES IN JUSTICE AND PUBLIC SAFETY EXPENSES** ABOVE THE OVERALL RISE IN PRICES BETWEEN 2007 AND 2013.

Map 3: Justice and Public Safety Expenses Increased in Most Counties

Growth Rate of Justice and Public Safety County Expenses, Inflation-Adjusted, 2007-2013



Note: The counties marked in grey fit into one of the following categories: do not have county governments, do not report their financials with basic financial statements or their statements of activities for 2007 and/or 2013 were not available. For more on the methodology, see the Methodological Appendix and the report Counting Money: State and GASB Standards for County Financial Reporting.

Source: NACo analysis of data from the statement of activities in 2007 and 2013 audited county financial statements

Provision of community health and human services is another core function for counties. In general, these costs comprised 11 percent of county expenses in 2013, before significant implementation of the Patient Protection and Affordable Care Act — commonly referred to as the Affordable Care Act (ACA).

36% OF COUNTIES WERE COPING WITH **RISES IN** THEIR **HEALTH AND HUMAN SERVICES COSTS ABOVE** OVERALL **INFLATION** BETWEEN 2007 AND 2013.

These costs exceeded 40 percent of expenses for a majority of counties in California, New Hampshire and New York. As administrative arms of state governments, counties serve as a safety net for low-income residents and their investment supports education, job training, childcare and housing, among many other programs that reach county residents of all ages. In addition, counties provide hospital care for individuals without any health insurance or ability to pay and they invest in health services for residents including health departments, hospitals, clinical care and behavioral care units. Between 2007 and 2013, 36 percent of counties were coping with increases in health and human services costs above overall inflation. Small counties (with less than 50,000 residents) were more likely to experience these increases. Health and human service costs in the majority of counties in Colorado, Louisiana, Montana, North Dakota and Texas grew faster than overall inflation.

Transportation and infrastructure are core responsibilities for many counties, often mandated by the state. Counties cover the entire gamut of infrastructure services, including owning and maintaining roads and bridges, providing public transportation, owning and operating airports and seaports, handling water supply, diverting storm water and waste management. Most often, transportation and infrastructure represent about 16 percent of total expenses for a county, but exceed one third of expenses for a majority of counties in Alabama, Delaware, Iowa and North Dakota. Between 2007 and 2013, transportation expenses rose faster than the inflation rate in more than half (54 percent) of counties; likewise, water, sewage and solid waste costs rises exceeded overall price changes in 44 percent of counties. Small counties (with less than 50,000 residents) were more likely to see an escalation in transportation expenditures. Transportation expenses rose the most in North Dakota counties, driven by oil and gas production needs.

THE MAJORITY OF COUNTIES WITNESSED **TRANSPORTATION EXPENSES RISING FASTER THAN INFLATION** BETWEEN 2007 AND 2013.

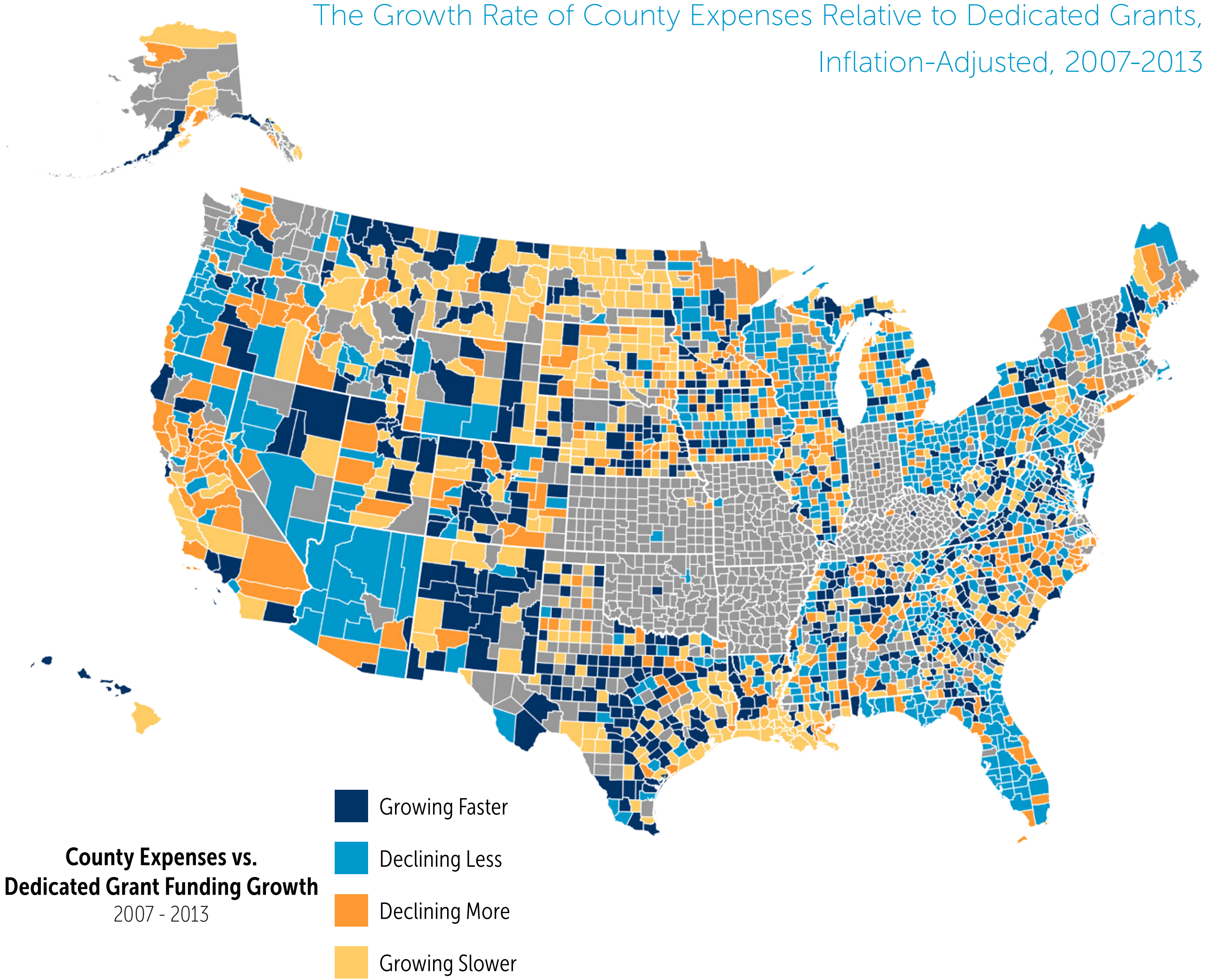
The rising costs of mandated services drive up the expenses for operating county governments. General government activities are essential services, either mandated by the state (such as assessing property values, issuing birth certificates and marriage licenses or collecting property taxes for schools, cities and others) or necessary to operate an organization (having a finance department, for example). As a result of the increasing needs of residents and the pressure to meet state and federal mandates, the general government expenses rose above inflation in about half (51 percent) of counties between 2007 and 2013. Counties are struggling to fund mandated and vital services, while maintaining a high level of service quality for residents.

3 STATE AND FEDERAL FUNDING IS INCREASINGLY INSUFFICIENT TO COVER FOR MANDATED COUNTY SERVICES.

No two counties are the same. Most often, states decide the role, structure and responsibilities for counties. As a result, counties differ in regards to the type and volume of services provided to residents. Counties are governed by locally elected officials and, in some instances, operate under home rule authority, which allows for more local flexibility and control with structural, functional and fiscal powers. Even within a state, counties vary in terms of services, depending on the availability of services from other levels of government, population size and density and extent of federal lands.

Map 4: Dedicated Grants Cover a Smaller Share of County Expenses

The Growth Rate of County Expenses Relative to Dedicated Grants, Inflation-Adjusted, 2007-2013



Note: The counties marked in grey fit into one of the following categories: do not have county governments, do not report their financials with basic financial statements or their statements of activities for 2007 and/or 2013 were not available. For more on the methodology, see the Methodological Appendix and the report Counting Money: State and GASB Standards for County Financial Reporting.

Source: NACo analysis of data from the statement of activities in 2007 and 2013 audited county financial statements

Many county services are mandated by the states or the federal government. State and federal governments provide different levels of funding to counties to pay for mandated services, frequently in the form of earmarked grants for operational expenses or capital expenditures of specific activities. Most often, about 93 percent of the state and federal funding used by a county is restricted to specific functions (called "dedicated grants" in this study); the remainder is part of general revenues.[12]

Dedicated grants funded a smaller share of county expenses in the majority of counties (59 percent), as a result of expense growth in excess of the increase in dedicated grants or costs declining less than funding from dedicated grants between 2007 and 2013 (Map 4). A majority of counties in states such as Florida and Tennessee recorded drops in the share of their expenses covered by dedicated grants.

59% OF COUNTIES RECORDED DEDICATED **GRANTS COVERING A SMALLER PERCENT OF COUNTY EXPENSES** IN 2013 COMPARED TO 2007.

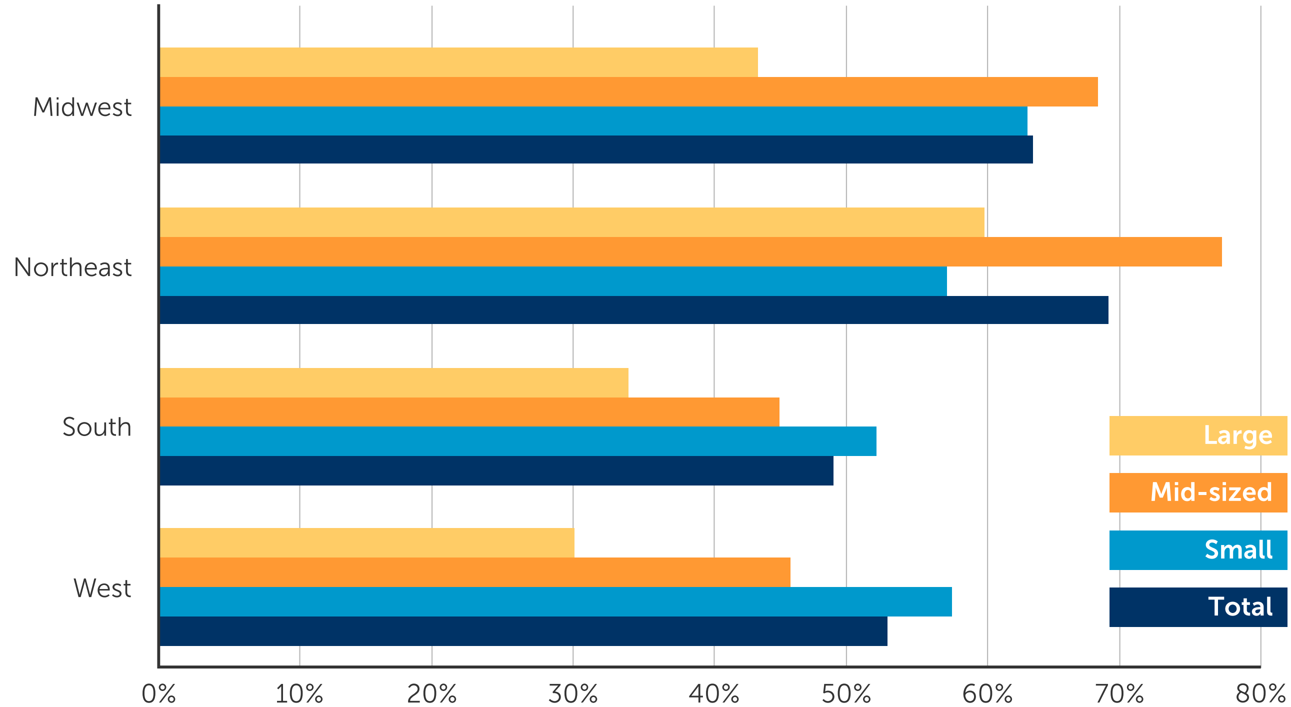
The decline in earmarked state and federal grants affected county services to varying degrees. For the majority of counties, dedicated grants covered the highest proportion of costs for transportation, at 43 percent of operational expenses and capital expenditures in 2013. In contrast, earmarked grants funded about 30 percent of county health and human services and 7 percent of justice and public safety. By 2013, dedicated grants funding covered a smaller percentage of expenses for both justice and public safety and community health and human services than six years before. A majority of counties in Virginia experienced declines in dedicated grants for justice and public safety relative to their restricted expenses between 2007 and 2013.

Counties fund mandated services more and more with general revenues and charges to compensate for declining coverage by state and federal funding. By 2013, general revenues funded 62.5 percent of county expenses, an increase of 1.5 percentage points in the funding share from the prior six years. The majority of counties (55 percent) experienced this trend. In states such as Wisconsin, Ohio, Iowa and Pennsylvania, more than 80 percent of counties funded a greater percentage of county expenses through general revenues compared to 2007 (Figure 2).

55% OF **COUNTIES** HAVE GENERAL REVENUES **PAYING A LARGER SHARE OF EXPENSES**.

FIGURE 2: GENERAL REVENUES FUND A LARGER SHARE OF COUNTY EXPENSES

Percent of Counties with Rising Shares of County Expenses Funded by General Revenues, Inflation-Adjusted, 2007-2013



Notes: Large counties have more than 500,000 residents; small counties have less than 50,000; and mid-sized counties are in between, based on 2015 U.S. Census Bureau population estimates. For more on the methodology, see the Methodological Appendix and the report Counting Money: State and GASB Standards for County Financial Reporting.

Source: NACo analysis of data from the statement of activities in 2007 and 2013 audited county financial statements

Charges, such as water rates, are user fees paid for a specific service and are restricted to fund expenses related only to that service. Most often, they cover about 18 percent of county expenses, mainly expenses for utilities and water, sewerage and solid waste. Between 2007 and 2013, charges revenues funded a higher proportion of county expenses in 45 percent of counties. In some counties, raising user charges is limited by the state. For example, in Iowa, county fees are established by the state legislature and counties do not have the statutory authority to raise them. Service charges are not an option for many counties, as these fees may also be established by the state legislature and counties may not the statutory authority to raise them either. Almost two thirds of counties in North Carolina, Ohio and Tennessee are relying more on service charge revenues to fund their expenses. This trend is most evident in large counties (those with populations higher than 500,000), with 56 percent of them covering more of their county expenses with revenues from service charges.

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40%

OF **COUNTIES** HAD **LOWER** ENDING **BALANCES** SIX YEARS **AFTER THE START OF THE GREAT RECESSION**.

The recession and slow recovery affected counties' bottom line. Fewer counties could cover all their expenses in 2013 relative to before the recession. In 2007, 82 percent of counties achieved an annual surplus (positive change in net position), but by 2013 only 71 percent did so. The ending balances were also lower in 2013. Forty (40) percent of counties had lower ending balances, with the largest concentration in the Northeast.

Counties face a constrained fiscal environment that affects county services and residents. In light of declining federal and state aid, counties increasingly need to find other sources of funding to cover for increased expenses. Six years after the start of the Great Recession, general revenues in many counties were either still declining or just slowly coming back. Further, state limitations on counties' capacities to raise revenues through taxes and charges impede the recovery of general revenues. In a follow-up study, NACo will explore the constrained fiscal environment many counties face due to the proliferation of state and federal mandates to counties, coupled with state limitations on counties' abilities to raise revenues. The study will also provide insight into the solutions and innovations that help counties to maintain quality services for residents.

ENDNOTES

[1] For more on the state of county economies, see Emilia Istrate and Brian Knudsen, County Economies 2015-Opportunities and Challenges, NACo Trends Analysis Paper Series, Issue 5, 2016.

[2] For a detailed explanation of financial terms, how counties report their financials, variations around the country and methods of accounting, see Istrate et al. Counting Money: State and GASB Standards for County Financial Reporting, NACo Policy Research Paper Series, Issue 4, 2016.

[3] This report examines data from the statement of activities from the audited county financial statements of 2,112 counties reporting basic financial statements (85 percent of all counties with basic financial statements). The data refer to the primary county government expenses and revenues and do not include the financials of county dependents (component units). All the growth rates reported in this study are inflation-adjusted, using the state and local price index for government consumption expenditures and gross investment from the U.S. Bureau of Economic Analysis. For more on the methodology, see the Methodological Appendix and the report *Counting Money: State and GASB Standards for County Financial Reporting*.

[4] General revenues data analyzed in this study do not include investment income and revenues for sales of assets.

[5] Property tax revenues are not limited to residential property, but extends to any type of property from which the county collects property taxes.

[6] This study does not examine any changes in property tax rates, because the data from the statement of activities do not provide this piece of information.

[7] Justin Higginbottom, State Provisions for Property Reassessment, http://taxfoundation.org/article/state-provisions-property-reassessment

[8] See the case with Proposition 13 in California- "California Counties: Rising Costs and Caps on Revenue Capacity" in Istrate et al.,"The Road Ahead: County Transportation Funding and Financing," NACo Policy Research Paper Series, Issue 2, 2014.

[9] For more on the state of county economies, see Emilia Istrate and Brian Knudsen, County Economies 2015.

[10] County expenses are primary government expenses, including expenses for governmental activities and business-type activities.

[11] Justice and public safety expenses include expenses related to sheriff, police and related services (impound, task forces, general law enforcement and patrol); emergency management and medical services; 911 communications; fire protection; detention centers and related commissaries, stores and inmate services. Also included in this class are judicial functions: judges; attorneys; prosecutors; justices; court clerks; probate courts; courthouses; warrant services and law libraries.

[12] Dedicated grants include county operating grants and contributions and capital grants and contributions. County expenses are primary government expenses, including expenses for governmental activities and business-type activities.

ACKNOWLEDGMENTS

Within the National Association of Counties, the authors would like to thank Michael Belarmino, Matt Chase, Joel Griffith, and Kathy Nothstine for their helpful comments and contributions. For their substantive comments on a draft of the report, the authors thank Emily S. Brock, Director, Federal Liaison Office of the Government Finance Officers Association (GFOA); Veronica Ferguson, County Administrator, Sonoma County, Calif., and President-elect of the National Association of County Administrators (NACA); David Douglas Lasher, County Treasurer, Clark County, Wash., and National Association of County Collectors, Treasurers and Finance Officers (NACCTFO) representative on NACo Board of Directors; William R. Peterson, Robin Harlow and Lucas Beenken from the Iowa State Association of Counties (ISAC). We are indebted to Tadas Pack for his assistance along every step of the way from data collection through analysis. A big thanks goes to all the interns who collected the audited county financial statements over the years, without which this research would not have been possible. The authors also express their appreciation to their Public Affairs colleagues for the graphic design, the interactive maps and the website of the report.

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ABOUT NACo

The National Association of Counties (NACo) unites America's 3,069 county governments. Founded in 1935, NACo brings county officials together to advocate with a collective voice on national policy, exchange ideas and build new leadership skills, pursue transformational county solutions, enrich the public's understanding of county government and exercise exemplary leadership in public service.

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Through NACo, county officials:

- Advocate with a collective voice on national policy
- Exchange ideas and build new leadership skills
- Pursue transformational, cost-effective solutions
- Enrich the public's understanding of county government, and
- Exercise exemplary leadership in public service.

Vision

Healthy, vibrant and safe counties across the United States.

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