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For Once, the Federal Government Really Was Here to Help.

The pandemic sent municipal revenues into a tailspin. They still haven't fully recovered, but $65 billion from Uncle Sam is easing a lot of pain.

Revenue growth for Philadelphia was so strong heading into 2020 that Marisa Waxman, the city's budget director, felt a little bit like Oprah Winfrey.

"We were so far ahead of estimates, we were bracing for a fight over what to do with all the extra money," she says. "You get a trash truck! You get a street sweeper! You get a tax cut! It was amazing."

The giddy feeling of plenty didn't last. Once the pandemic hit, the city's revenues dried up. Everything but health, public safety and schools came in for cuts. "We had three amazing quarters," Waxman says. "Then the bottom fell out."

It was the same story all over. Cities headed into the pandemic finally witnessing their inflation-adjusted revenues rise above levels last seen in 2007, before the Great Recession. Those gains were wiped out by the pandemic and its immediate shock to the economy.

But revenues turned out not nearly as bad as they could have been. The economy rebounded and remote workers were able to keep spending and paying income taxes. And there were other factors that saved municipal bacon.

Most notably, the American Rescue Plan Act (ARPA), enacted in March, provided $65.1 billion in direct relief for cities, towns and villages. Federal funds were cited by 81 percent of fiscal officers as their single most-positive factor in putting together their fiscal 2021 budgets, according to the National League of Cities' annual city fiscal conditions survey, released Tuesday.

"Cities ended fiscal year 2020 with a revenue loss – the first since the Great Recession – and they budgeted even larger decline for fiscal 2021," says Christiana McFarland, NLC's research director. "These losses pale in comparison to what they could have been without federal intervention."

ARPA was a godsend, but it hasn't solved all problems. In fact, cities and states have been slow to allocate those dollars. Large cities have spent just 8.5 percent of the funds they've received so far, while states have spent only 2.5 percent, according to an Associated Press analysis.

Philadelphia is using all of its $1.4 billion worth of ARPA money to make up for lost revenues over the next several years. Waxman admits it's not a very satisfying decision for residents. No new street sweepers, no new trucks.

"It's new money for old stuff," she says. "ARPA dollars can be spent into 2024, so we're drawing them down over a number of fiscal years as a glide path to allow our other revenues to recover."

Where Taxes Are Collected

Cities caught another break heading into the pandemic. In 2018, the Supreme Court ruled that states could collect taxes on sales from vendors without a physical presence within their borders. The Wayfair decision allowed cities and states to collect billions in revenues that otherwise would have been lost as consumers shifted more of their spending online. “Wayfair was a wonderful, fortuitous decision by the Supreme Court, and a good one,” says Michael Pagano, a municipal finance expert at the University of Illinois Chicago.

Depending on their economic mix, some cities benefited from shifts in the economy. Being home to Procter & Gamble – maker of Bounty, Charmin and many other consumer goods – helped Cincinnati’s bottom line.

“I guess I should thank everyone who ordered toilet paper, but we had some very strong corporate profits that were completely unanticipated,” Andrew Dudas, Cincinnati’s budget director, said during a webinar announcing NLC’s fiscal findings.

Not every ball bounced Cincinnati’s way, however. Corporate and personal income taxes make up more than 70 percent of the city’s revenues. When the bottom fell out in the spring of 2020, the city opened up a $50 million line of credit, since Ohio allows cities to borrow in emergencies to pay for basic services.

Thanks to ARPA, Cincinnati didn’t have to take on that debt. The city is using just over 75 percent of its ARPA money to make up for lost revenues. The rest is going to help businesses that were hit hard by the pandemic.

Since property tax collections are capped at $29 million, Cincinnati is losing out on the increase in residential property values. Meanwhile, like every other city with a central business district, it has to worry about what percentage of the workforce will be coming back to the office, and when.

“We’re estimating around 16 percent permanent reduction to our income tax due to remote work,” Dudas says. “We’ve had some corporations downtown that have brought significant numbers of employees back, but it’s nowhere near where it was pre-pandemic.”

Waiting on Infrastructure

Everyone is wondering how the economy will be restructured, which raises a chicken-and-egg question: Should cities plan to change their tax codes to reflect the new reality, or do they have to wait and see what the new reality might look like in order to figure out how to capture their share? “After this pandemic, no one knows, but we are definitely thinking about it,” says Susan Gooding-Liburd, chief financial officer for Miramar, Fla.

In Philadelphia, remote workers typically make up 40 percent of the city’s earned income tax base. “When we projected our revenue losses across a five-year plan, it is still more than $1.4 billion,” Waxman says. “We’re envious of cities with a property tax.”

Two-thirds of the 444 cities analyzed by NLC have prioritized replacing lost revenue with ARPA funds, while 54 percent are also helping out individuals, businesses and nonprofits hurt by the economic impact of the pandemic.

Cities are all over the place in terms of their current fiscal well-being. For fiscal 2021, 18 percent of cities budgeted for revenue growth above 5 percent, while 29 percent budgeted for greater than 5 percent decline. That kind of range is unusual, McFarland says.

Infrastructure was the category named by most finance officers as negatively affecting their 2021 budgets. Many projects were put on hold by the downturn.

Revving them up might take some time. If and when Congress approves an infrastructure package, finding enough engineers and skilled laborers to do the work is going to be a challenge, Waxman says, given the booming construction market. Meanwhile, the rising cost of materials means money won't go as far as it would have when many plans were first drawn up.

Still, a trillion or so in federal infrastructure dollars would allow cities to dream big, rather than simply trying to keep their collective heads above water. "We're trying to make sure we're positioning ourselves to be able to stand on our own two feet," Waxman says, "after the federal money draws down."

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October 06, 2021 • Alan Greenblatt