Local tax limitations can hamper fiscal stability of cities and counties

3 ways states can help localities improve budget flexibility and resiliency

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About Pew

Pew is a global nonprofit, nonpartisan public policy organization that conducts research and advocacy on issues including public health and safety, consumer finance, state and local fiscal health, and the environment.
Local Tax Limitations Can Hamper Fiscal Stability of Cities and Counties

3 ways states can help localities improve budget flexibility and resiliency
The landscape of local tax limitations

States have long history of restricting local taxes

• Limits exist on the tax rate, tax base, total revenue collected, and revenue use.

• Many localities face multiple constraints.

• Limits may not be the same for cities and counties.

• Some limits can be overridden by the local governing body but many require state or voter action.
How cities and counties raise their tax dollars

New England states rely heavily on property taxes

Source: Pew analysis of U.S. Census Bureau data
Local tax limitations can create ratchet-down effect
Constraints can hamper pace of local revenue growth after recession

Without ratchet effect, revenue is able to bounce back after a temporary drop

With ratchet effect, a temporary drop becomes a permanent reduction in cap
Local tax limitations can hinder long term fiscal stability

Limits narrow the ways local leaders can respond to fiscal crises, community needs

• Limits may prevent revenue growth from keeping up with service demands or even inflation.

• Limits can worsen geographic disparities.

• Few revenue alternatives may increase tax burdens.

• Limits can force local officials to make decisions that make the community less desirable, further eroding the tax base.
Ways to mitigate impacts of local tax limitations
States can lift restrictions during fiscal crises

Temporarily lift restrictions during fiscal crises such as recessions to give localities more tools to address them.

Examples: New Jersey, Pennsylvania
Ways to mitigate impacts of local tax limitations
Adjust limitations to allow for recession recovery

Ensure limits do not prevent local revenue from recovering after a recession so localities can restore services.

Examples: Colorado, Maryland

Dolores, Colorado
Ways to mitigate impacts of local tax limitations
Increase local budget flexibility in the long term

- Update state sales tax base to reflect changes in economy.
- Support service sharing among localities.
- Evaluate tax limits and policy goals.

Local governments can share emergency response services to limit costs.
Key takeaways on local tax limitations
Ways to mitigate effects, improve long-term budget sustainability

1. Limitations on local taxation can impede local recession recovery as well as long-term fiscal stability.

2. States can consider revising limitations to give local governments more tools for handling an economic downturn.

3. States can also think about ways to increase local budget flexibility in the long term.