

COVID-19 will likely lead to a recession. Can Massachusetts municipal budgets handle one?

By Andrew Mikula, Peters fellow

For many, March 2020 was eerily similar to [September 2008](#), at least in one way. Economic uncertainty reached all corners of society. Unemployment claims [soared](#) in all 50 states, and small businesses [shut down](#) left and right.

But while the federal government has [unfathomable financial clout](#) during this crisis, local governments [do not](#). In the aftermath of widespread shuttering of businesses, some municipal revenue streams will be devastated while others remain stable.

For example, the effect of the Great Recession on property taxes was both [lagged and diminished](#) relative to its impact on property *values*. This is largely because property taxes are calculated based on past years' data, and changes in real estate assessments are often phased in. The main concern with property taxes for many communities will likely be difficulty collecting from cash-strapped families, not a decline in value given existing formulas. While legislation like [Proposition 2.5](#) has rightly ensured that towns and cities can't tax their way out of a budget shortfall, they may not need to try in the first place. Revenue from property taxes remained stable throughout the Great Recession.

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This is good news, as property taxes make up the majority of [revenue streams](#) in 89 percent of Massachusetts municipalities. Still, the other 11 percent include some of the state's poorest communities, reliant on state revenues to balance budgets and vulnerable to business cycle volatility (see Figure 1). The top five recipients of [state revenue per capita](#) are Lawrence, Springfield, Chelsea, Brockton, and Holyoke, in that order.

Meanwhile, the state [largely relies](#) on income and sales taxes to fill its coffers. As businesses shutter and workers are laid off, revenue from these taxes will likely decline, as [during the Great Recession](#) (see Figure 2). After facing budget cuts in 2009, Massachusetts lawmakers [boosted the sales tax rate](#) from 5 percent to 6.25 percent, prolonging the state's reliance on volatile revenue sources.

Many municipal coffers would also suffer during a prolonged recession. If COVID-19 continues to disrupt daily life for several months, the virus could influence [crucial legislative votes](#) on the state budget over the summer. Just like during the 2008 financial crisis, aid to local governments could take a hit. From 2008–2010, the amount the legislature allotted for local aid [declined by 28 percent](#), even while overall spending grew. In Fiscal Year 2020, local aid spending remains 12 percent below its 2008 peak.



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Figure 1: 2017 municipal revenues by category among the least tax-reliant communities in MA

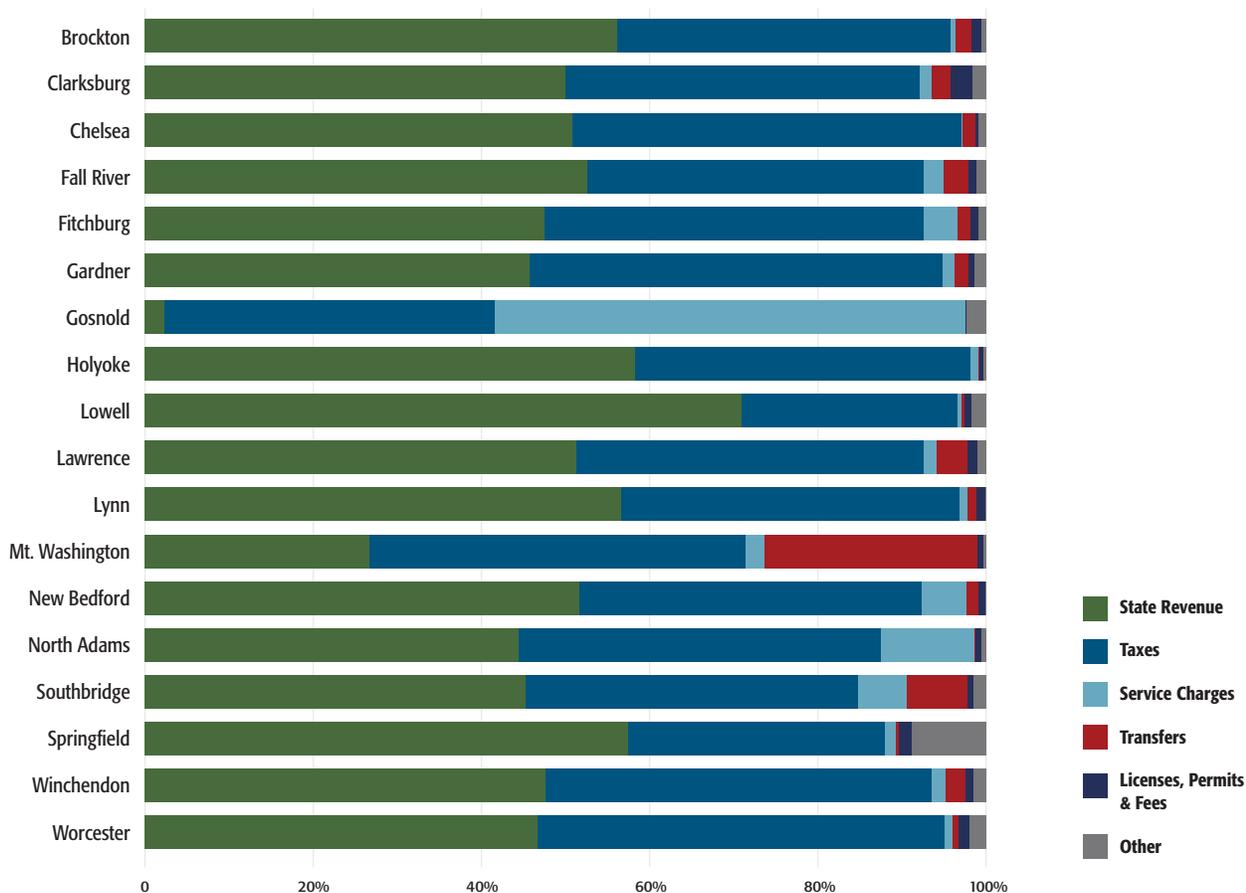
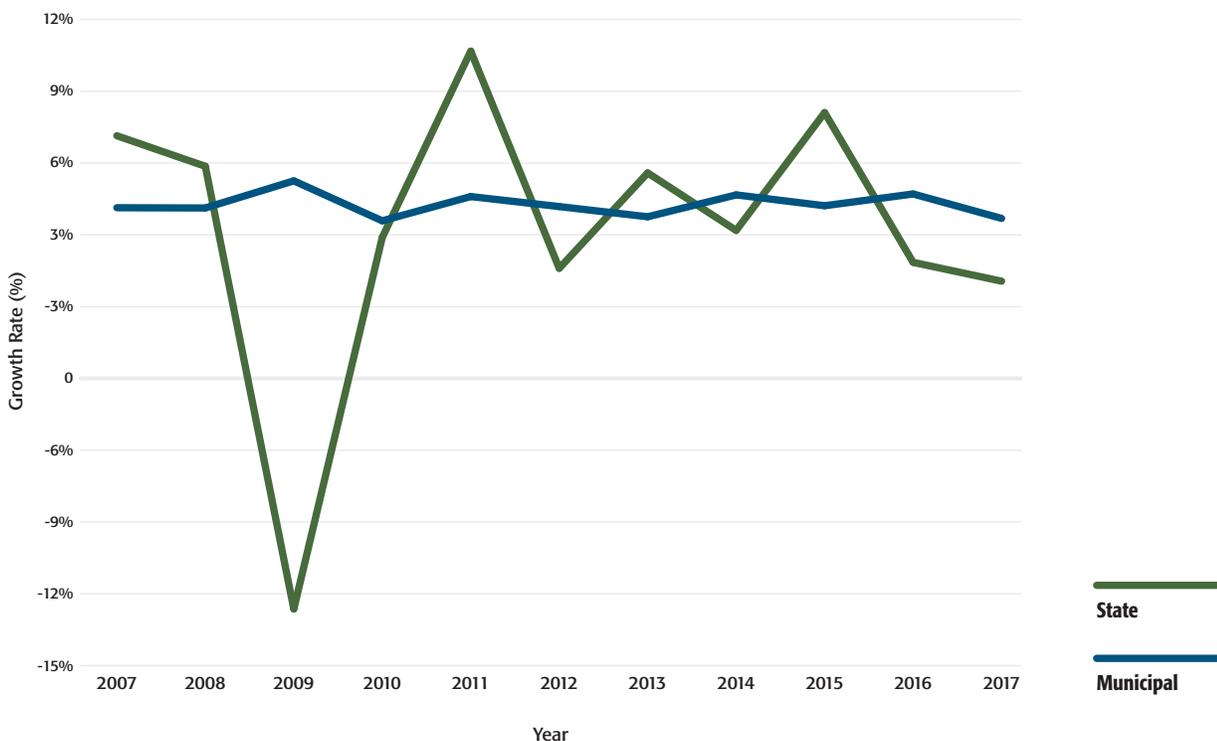


Figure 2: Tax revenue growth rate in Massachusetts state and local governments, 2007–2017



Other municipal revenue sources have their own problems. Revenue from licensing and impact fees is small, and also depends on consumers and small businesses in a way that is unreliable during a recession. With fewer people out shopping or taking vacations, communities that rely more on revenue from business licenses, beach stickers, and parking violations may respond by [getting stricter](#) about pricing and enforcement. From 2012–2016, as the nation recovered from the Great Recession, the number of speeding tickets issued in Massachusetts declined by 26 percent.

Still, changes in local law enforcement and fees are often guided by [state policy](#), and only 18 percent of Massachusetts communities got more than a tenth of their revenue from non-tax, non-state sources in 2017. These figures bolster the importance of the fact that state grants are the only major municipal revenue source that [consistently dries up](#) during hard times.

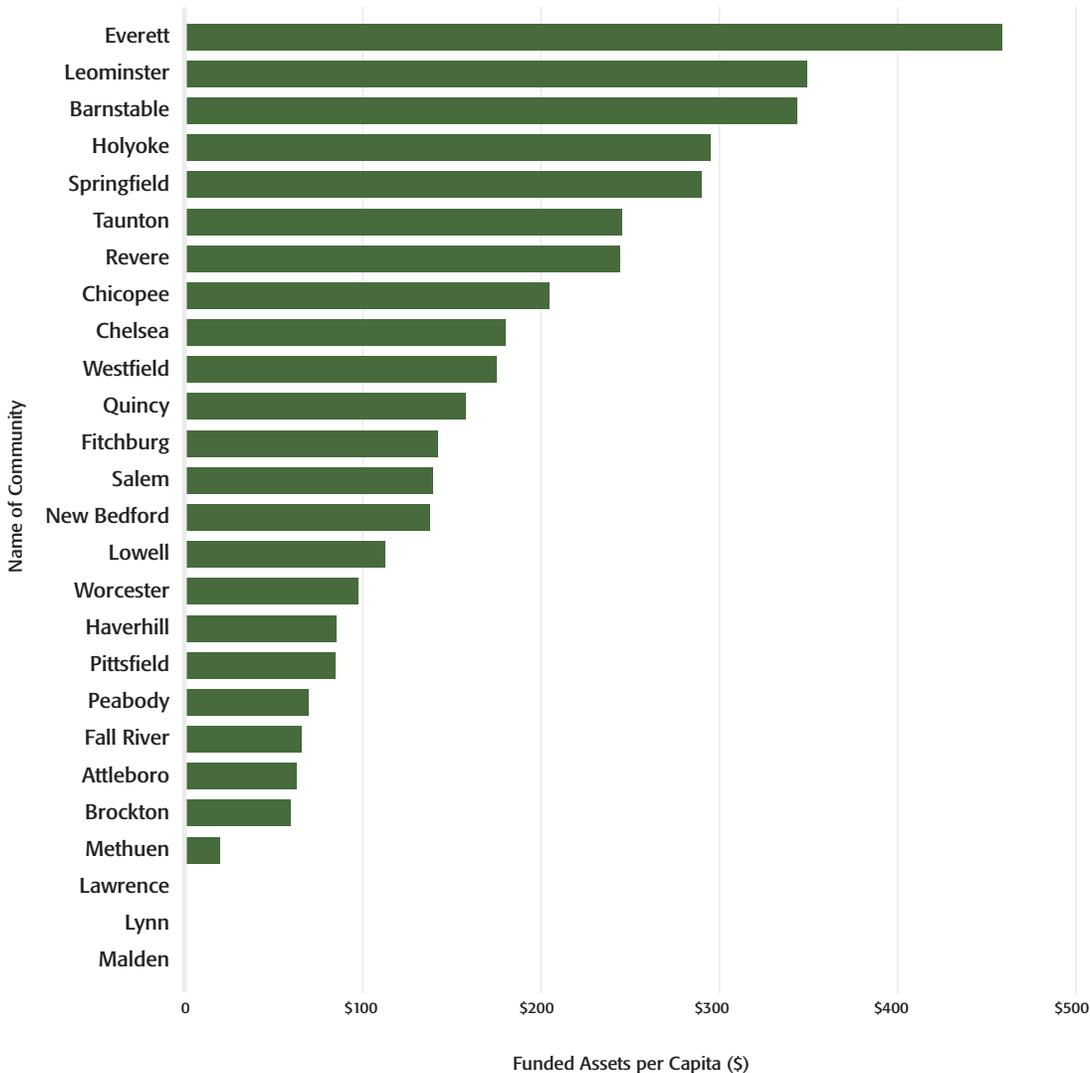
Many communities reshuffle their financial assets in order to

close deficits, and in 2017, 61 percent of Massachusetts municipalities reported at least \$1 million in stabilization (“rainy day”) funds. In Gateway Cities, stabilization funds contained some [\\$142 per capita](#), providing some benefit for communities that disproportionately rely on state revenues to fill their coffers (see Figure 3).

Public works and culture & recreation are the only expenses that were [consistently cut](#) from municipal budgets during the Great Recession. Historically, foregoing roadway and park maintenance rather than cutting school or public safety funding has been more palatable for communities.

This time, it’s unclear whether local governments will face these kinds of tradeoffs, especially if the nation bounces back from COVID-19 quickly. The challenge for many municipal officials is that the state of their finances next year largely depends on management (whether fiscal or pandemic-related) at the state and federal levels.

Figure 3: Stabilization fund assets per capita among Massachusetts Gateway Cities, 2017



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