Financing Municipalities in New England: Revisiting the State-Local Relationship

New England Public Policy Center
Conference Report 07-1
June 2008
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Executive summary
On December 5, 2007, the New England Public Policy Center at the Federal Reserve Bank of Boston held its third annual policy symposium, “Financing Municipalities in New England: Revisiting the State-Local Relationship.” Through presentations and a panel discussion, the conference brought together legislators, business leaders, researchers, and policy advisors to examine the long-term fiscal challenges facing the region’s municipalities, and to discuss potential revenue solutions. This report provides an overview of the conference’s major themes:

• **The structure of local government in New England is unique.** In contrast to the rest of the country, cities and towns in New England are largely responsible for providing the entire range of local services, including schooling, as counties are limited or nonexistent. The region also relies more heavily on property taxes and less on other tax revenue and charges and fees than do other areas of the country.

• **New England’s municipalities face long-term fiscal challenges.** The cost of providing public services is growing faster than the ability of state and local governments to raise revenues. And with an aging population and rising health care costs, fiscal pressures are likely to continue to grow. A larger percentage of the population will be older in New England than in the nation in coming decades, leading to greater demand for health care, pensions for retired government employees, and other age-related costs. On the other hand, a projected decline in the school-age and college-age population shares implies reduced demand for educational services, somewhat offsetting the burdens of an aging population. However, as states experience budgetary pressures from future aging and health care cost trends, they may respond by cutting local aid. If that were to occur, municipalities would face an even more difficult fiscal situation.

• **State-local collaboration is critical to addressing the ongoing municipal fiscal challenges.** As state and local governments are inextricably linked, solving municipal fiscal problems will require a long-term commitment by both state and local governments. All parties will have to consider the interests of others and be willing to make compromises.
• Potential sources of additional revenue for New England municipalities exist but possess drawbacks. State and local policymakers may consider alternative revenue sources for municipal governments, such as local-option sales taxes. Local sales taxes have growth potential, but they are more volatile than property taxes and are feasible only for communities where there is a significant sales base that can be taxed. Another possible solution is changing state aid formulas to more intensively target communities in greater fiscal distress. Because there is no “one-size-fits-all” solution, states and municipalities will need to collaborate and consider a mix of policy tools and each state’s unique situation in order to address the ongoing municipal fiscal challenges in the New England states.
Municipalities are of particular importance in New England, because they are typically responsible for the entire range of local services, including schooling. Yet municipalities are facing serious fiscal stress as revenues fail to keep pace with the growing cost of providing services amid rising demand. State-local collaboration is critical to addressing these challenges, as cities and towns seek new ways to generate more revenues and control costs.

Overview

The dynamic between municipal revenue sources and the state-local relationship in New England.

Richard Dye, Professor of Government and Public Affairs at the University of Illinois at Chicago, and Visiting Fellow at the Lincoln Institute of Land Policy in Cambridge, Massachusetts, provided an overview of the relationship between state and local governments in New England, and a broad outlook for fiscal pressures on states and municipalities.

Dye noted that the New England region has a unique structure of local government. City and town governments in the region provide public services that counties or special-purpose districts provide elsewhere. For example, New England states are more likely to provide public schooling through municipal governments, whereas much of the rest of the nation relies on independent school districts. Nationally, counties collect one-quarter of local government revenues, yet county governments play an insignificant role or are non-existent in New England. In Maine and New Hampshire, counties account for only 3.1 and 8.8 percent of local revenues, respectively (see Table 1). County governments are of trivial importance in Massachusetts and Vermont, and do not exist in Rhode Island and Connecticut.

CITIES AND TOWNS IN NEW ENGLAND RELY MORE HEAVILY ON PROPERTY TAXES AND LESS ON OTHER TAX REVENUES THAN DO LOCAL GOVERNMENTS IN OTHER REGIONS. FOR EXAMPLE, LOCAL PROPERTY TAXES ACCOUNTED FOR JUST 27.9 PERCENT OF TOTAL LOCAL REVENUES NATIONALLY IN FISCAL YEAR 2005 (FY2005), THE LATEST YEAR FOR WHICH OFFICIAL STATE-SPECIFIC DATA ARE AVAILABLE. HOWEVER, IN NEW ENGLAND THAT SHARE RANGED FROM 43.8 PERCENT IN MASSACHUSETTS TO 55.9 PERCENT IN CONNECTICUT, WITH THE EXCEPTION OF VERMONT AT 16.9 PERCENT. THE STATE GOVERNMENT OF VERMONT HAS ASSUMED A LARGE PORTION OF THE PREVIOUSLY LOCAL PROPERTY TAXES SINCE 1998, RESULTING IN LESS PROPERTY TAX REVENUE LABELED

<table>
<thead>
<tr>
<th>Percent</th>
<th>US</th>
<th>CT</th>
<th>ME</th>
<th>MA</th>
<th>NH</th>
<th>RI</th>
<th>VT</th>
</tr>
</thead>
<tbody>
<tr>
<td>County</td>
<td>25.2</td>
<td>0.0</td>
<td>3.1</td>
<td>0.9</td>
<td>8.8</td>
<td>0.0</td>
<td>0.3</td>
</tr>
<tr>
<td>Municipal</td>
<td>28.0</td>
<td>37.3</td>
<td>26.4</td>
<td>44.2</td>
<td>27.9</td>
<td>50.3</td>
<td>9.6</td>
</tr>
<tr>
<td>Township or town</td>
<td>3.3</td>
<td>54.4</td>
<td>39.6</td>
<td>36.5</td>
<td>19.3</td>
<td>40.6</td>
<td>19.8</td>
</tr>
<tr>
<td>Special district</td>
<td>9.1</td>
<td>5.1</td>
<td>6.9</td>
<td>11.6</td>
<td>2.5</td>
<td>4.7</td>
<td>4.6</td>
</tr>
<tr>
<td>School district</td>
<td>34.4</td>
<td>3.2</td>
<td>24.0</td>
<td>6.8</td>
<td>41.5</td>
<td>4.4</td>
<td>65.7</td>
</tr>
</tbody>
</table>

as local. Those state property tax revenues have been redistributed to school districts through a more equalizing education aid formula.

Municipalities in New England have limited access to local-option taxes and rely relatively little on non-tax sources of revenue such as fees and charges. For example, fees and charges represented 16.0 percent of local government general revenue nationwide in FY2005, but in New England ranged from only 6.8 percent in Connecticut to 10.7 percent in Maine.

State aid is the second largest source of local government revenue in all New England states but Vermont, ranging from 28.4 percent in Maine to 35.8 percent in Massachusetts in FY2005. In Vermont, state aid accounts for 67.2 percent of local revenue, because, as previously noted, the state collects and distributes a state property tax under an aid formula designed to help equalize school spending.

In 2002, many states nationwide began to experience dramatic declines in state revenue collections because of the 2001 recession. During this fiscal crisis, some of these states, including Massachusetts, reduced aid to local governments. Some evidence suggests that cities and towns responded to the state aid cuts by imposing higher property taxes. For example, in a 2007 national study, Dye and Andrew Reschovsky found that, on average, for every one-dollar cut in state education aid, local property taxes rose 25 cents. However, some states, including Maine, Massachusetts, and Rhode Island, limit annual increases in local property taxes. These limitations heighten the importance to municipalities of state aid and their access, or lack thereof, to non-property tax based local revenue sources.

Future changes in the age profile of the region’s population will create even greater fiscal challenges for New England cities and towns. Nationwide, the elderly share of the population (individuals age 65 and older) is projected to rise from 12.4 percent in 2000 to 19.7 percent in 2030 (see Table 2). This shift will be even more pronounced in New England. Vermont and Maine will be most affected, with the elderly population shares projected to be 24.4 and 26.5 percent in 2030, respectively.

These changes mean that for state and local governments, health care, unfunded pension liabilities for government employees, and other costs related to elderly population are likely to rise. As baby boomers near retirement, cities and towns face health care pressures from funding local government retirees’ medical insurance. At the state level, similar health care pressures from government retirees, combined with rising Medicare costs, stress state budgets. Under such budgetary pressures, states may not be able to provide the same level of local support in the future and may further shift responsibilities for providing public services to the local level.

An aging society is not all bad news for state and local governments. The school-age and college-age shares of the population are projected to decline in coming decades, especially in the New England states. This is likely to reduce demand for public school services and therefore somewhat offset the burdens of an aging population. However, as states face increasing pressures on their budgets from future demographic and health

<table>
<thead>
<tr>
<th>Percent</th>
<th>2000</th>
<th>2030 (projections)</th>
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<tbody>
<tr>
<td>United States</td>
<td>12.4</td>
<td>19.7</td>
</tr>
<tr>
<td>Connecticut</td>
<td>13.8</td>
<td>21.5</td>
</tr>
<tr>
<td>Maine</td>
<td>14.4</td>
<td>26.5</td>
</tr>
<tr>
<td>Massachusetts</td>
<td>13.5</td>
<td>20.9</td>
</tr>
<tr>
<td>New Hampshire</td>
<td>12.0</td>
<td>21.4</td>
</tr>
<tr>
<td>Rhode Island</td>
<td>14.5</td>
<td>21.4</td>
</tr>
<tr>
<td>Vermont</td>
<td>12.7</td>
<td>24.4</td>
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</table>

Given these likely future developments, Dye pointed out a need to consider policy responses, such as changes in formulas for distributing state aid to cities and towns in order to better target those most in need, or alternative revenue sources for municipal governments.

### Potential revenue strategies and solutions

#### Designing state aid formulas to address local non-school fiscal distress

With many cities and towns in New England facing considerable fiscal distress, one potential solution is to increase state aid. However, existing aid formulas may not address local fiscal distress appropriately. Bo Zhao, an economist with the New England Public Policy Center at the Federal Reserve Bank of Boston, discussed research he has undertaken to develop a new aid formula that would target municipal (non-school) aid more precisely to needier communities. His analysis uses Massachusetts as a prototype, but his research framework, methods, and policy principles are potentially applicable to other states.

Zhao and his coauthor, Katharine Bradbury, also of the Boston Fed, first measured local fiscal distress by comparing the unavoidable costs that cities and towns must incur when providing basic services with their capacity to raise revenue from local sources. Unavoidable costs are those determined by social and economic characteristics that are outside the control of local governments. Analyzing data from Massachusetts, Zhao and Bradbury found that higher unavoidable costs for providing municipal services are associated with higher population densities, unemployment rates, populations, jobs per capita, and poverty rates. Using prototypical Massachusetts communities, they found that large cities, job-center suburbs, and resort towns incur higher costs, while rural towns and high-income residential suburbs face lower costs (see Table 3).

Their statistical analysis revealed that a city or town’s ability to tap the residential property tax base under Proposition 2½—the Massachusetts law capping annual increases in property taxes—increases with residents’ income. They also took into account other local revenue capacity from non-residential property taxes, hotel/motel taxes, and motor vehicle excise taxes, which increase proportionally with the size of those tax bases. They then deducted the capacity that is “used up” for non-municipal purposes, such as the required local contribution to public schools and payments for regional transit, in arriving at each municipality’s measure of nonschool local revenue capacity. Again using prototype communities, Zhao and Bradbury found that large cities and rural towns have limited revenue capacity, while job-center suburbs, high-income residential suburbs, and resort towns tend to have greater capacity.

A local government’s cost-capacity gap equals its costs minus its revenue capacity.

#### Table 3. Per capita non-school cost-capacity gap of prototype Massachusetts communities

<table>
<thead>
<tr>
<th>In dollars</th>
<th>Average community</th>
<th>Large city prototype</th>
<th>Rural town prototype</th>
<th>Job-center suburb prototype</th>
<th>Higher-income residential suburb prototype</th>
<th>Resort town prototype</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-school cost</td>
<td>799</td>
<td>1,224</td>
<td>682</td>
<td>918</td>
<td>657</td>
<td>813</td>
</tr>
<tr>
<td>Non-school capacity</td>
<td>677</td>
<td>265</td>
<td>365</td>
<td>628</td>
<td>955</td>
<td>1,893</td>
</tr>
<tr>
<td>Non-school cost-capacity gap</td>
<td>122</td>
<td>959</td>
<td>317</td>
<td>290</td>
<td>-298</td>
<td>-1,080</td>
</tr>
</tbody>
</table>

Note: Data year is 2000 unless otherwise indicated. 
A larger gap indicates that the community is in greater fiscal distress. Among the prototype communities, large cities tend to have the highest positive gaps, while resort towns have substantial negative gaps, with other types of communities falling somewhere in between (see Table 3).

Based on the local cost-capacity gaps, Zhao and Bradbury developed a new formula that would better align municipal aid to communities with fiscal distress. The formula includes three built-in policy variables. The first is an aid floor: a certain amount of state aid for all communities. The second is a gap cutoff. A community is eligible for aid more than the aid floor when its cost-capacity gap is higher than the chosen gap cutoff. A gap cutoff is necessary for the formula because the statewide distribution of cost-capacity gaps may be wide and may involve negative gaps; it is practically impossible to distribute aid simply in proportion to the gap without setting a benchmark. The last variable is the total aid pool: the amount of state aid available for all communities.

Most states have in place some existing programs for providing aid to local governments, and they are often “held harmless” by either tradition or explicit legislation that guarantee, at a minimum, past dollar amounts in future years. The question of how to honor this hold-harmless guarantee poses a challenge when states are in transition to a new local aid formula. To address this challenge, Zhao and Bradbury propose an approach that takes account of both existing aid and new aid in filling local fiscal gaps. In doing so, the new aid formula is able to target communities with larger gaps and less existing aid. Using a five-year aid simulation, they showed that the formula can achieve a higher degree of fiscal equalization over time by filling an increasing portion of the local fiscal gaps with the combined existing and new aid (see Figure 1).

Understanding the impact of adopting local-option sales taxes

David Sjoquist, Professor of Economics at the Andrew Young School of Policy Studies at Georgia State University, presented another potential revenue solution to current municipal fiscal woes: local-option sales taxes.

Local sales taxes are an important source of revenue, equaling nearly 15 percent of total local property tax revenues in FY2005 in the United States. Sales taxes were introduced in the 1930s; New York City was the first municipality to adopt a sales tax, in 1934. Now 34 states allow local-option sales taxes. For example, in Georgia, counties...
can assess a 1 percent sales tax, while in California, municipalities can assess local-option taxes ranging from 0.125 percent to 1.5 percent, mostly earmarking them to fund transportation projects, libraries, and other public services.

In general, the importance of local-option sales taxes has increased over time. Revenue from local sales taxes and taxes on gross receipts grew from 1970 to the mid-1980s, primarily reflecting an increase in the number of states adopting local-option sales taxes (see Figure 2). That growth has since leveled off because only a few additional states have adopted such taxes. Local-option sales taxes have traditionally not been employed in New England.

Sales tax revenues have good growth potential. According to a study cited by Sjoquist, a 10 percent rise in the income of Massachusetts residents could lead to a 14 percent overall increase in sales tax revenue. However, because they are more cyclically sensitive, sales taxes are less stable than property tax collections.

Adopting a local-option sales tax can affect local government both on the revenue side and the expenditure side. Some studies show that an adoption of a local-option sales tax is associated with lower property taxes, but cities and towns differ in how much property taxes are reduced. On the expenditure side, researchers have reported mixed findings. One study that Sjoquist cited finds that some cities do not increase expenditures after adopting new local taxes, while others do.

Local-option sales taxes may also affect development patterns, which in turn can affect the need for local services. Local-option sales taxes can create greater inter-jurisdictional competition for retail, particularly shopping centers. One study finds that a 10 percent increase in state reliance on local sales taxes increased retail outside a metropolitan area’s central places by 2.4 percent. Another research paper using California data indicates that city managers consider retail as the most desirable form of land use based on potential sales tax revenues.

Local-option sales taxes also introduce potential equity issues. First, sales tax bases are not evenly distributed across communities. Furthermore, the burden of local-option sales taxes borne by nonresidents may exceed the value of the benefits that these nonresidents receive from programs financed by these taxes. For example, a small community with a large shopping center can capture large amounts of revenue from nonresidents; the host community then uses these revenues to finance its schools, which benefit only the children of its residents. A second issue is the degree to which local sales taxes distribute their burdens according to “ability to pay.” The retail sales component and sales tax on business purchases have a propensity to be regressive in nature (see Figure 3 on page 10). Lower-income individuals pay a larger proportion of their incomes on sales taxes than higher-income individuals, a violation of the “ability to pay” principle.

Policymakers need to ask an array of questions when considering adopting a local-option sales tax. How will it conform to the state tax base? Will the tax be the same in every community that adopts it, or will each be allowed to set the terms, promoting...
jurisdictional competition? Will the tax be collected at the origin of sale or the destination where the product is used? How is it collected and by whom? Is it the duty of state or local governments to collect and distribute? Policymakers should also be aware of the several alternatives to local-option sales taxes, including the local income or payroll tax, gross receipts tax, and excise taxes.

Responses from a panel of New England practitioners

The conference moved from research-oriented proposals for addressing municipal fiscal distress to a panel discussion addressing specific questions about how states and localities in New England are actually tackling this issue. The panel consisted of New England public officials and advocates with years of experience in dealing with the fiscal issues facing state and local governments:

Mary Clare Higgins, Mayor, City of Northampton, Massachusetts, and President of the Massachusetts Municipal Association

Leslie Kirwan, Secretary, Massachusetts Executive Office for Administration and Finance

John Piotti, Maine State Representative and House Chair of Maine’s Joint Taxation Committee

Gary Sasse, Executive Director, Rhode Island Public Expenditure Council (now Rhode Island’s Commissioner of Revenue)

Moderator: Andrew Reschovsky, Professor of Public Affairs and Applied Economics at the University of Wisconsin-Madison, and Visiting Fellow at the Lincoln Institute of Land Policy in Cambridge, Massachusetts.

This section provides an overview of the questions posed by the moderator and the answers provided by the panelists during the panel discussion.

Question 1: From your perspective, how serious are the fiscal problems facing local governments in your state? Do these problems exist only for relatively few of the local governments in your state, or are the problems widespread?

There was a consensus among the panelists that the fiscal problems facing local governments are serious and widespread.

Figure 3. Tax Burden (Massachusetts, 2002)

The problems are not only concentrated at the local level, but also affect state governments. Several of the panelists reported that the problem is structural—a result of growing expenditure needs and a revenue base that is unable to fund these growing needs—as opposed to cyclical (secular changes in the economy). The panelists from Massachusetts noted that the structural problems encountered were largely due to rising health care costs. As health care costs outpace state and local revenue growth, providing health care to current and retired public employees is broadening the gap between available revenues and all other expenses.

The panelists also noted growing discontent with the main local source of revenue in New England, the property tax. Taxpayers are unwilling to pay more in property taxes; as panelist John Piotti stated: “it is a stone that can’t be bled anymore.” At the same time, expenditure demands on governments relying on this revenue source are growing. Piotti noted that in some communities almost 90 percent of local property tax revenues finance the growing cost of secondary school education, leaving local governments with limited resources to pay for other services. Gary Sasse noted that local governments’ overdependence on the property tax is a result of the structure of the region’s entire state and local tax system, but that resolving this issue will be difficult given that there is little appetite for a tax system based on a broader array of taxes.

**Question 2:** What do you see as the future role of the property tax in your state? Are there proposals being considered to target relief to certain taxpayers who are really being burdened?

Several panelists reported that their state currently has tax relief programs. Maine has a targeted property tax relief program for households who are paying a significant percentage of their income in property taxes. That state also recently increased aid to municipalities for education to relieve local property tax burdens. However, many residents are not satisfied with the results.

Sasse reported that Rhode Island has recently adopted a limit on annual growth of property tax levies to 5½ percent. This cap will decrease by one-quarter of 1 percent annually until it reaches 4 percent in 2013. However, many communities have applied for permission to exceed the limit or are taxing at a level just below what is allowed. He expects that these communities will face fiscal stress in the future as the cap on growth in the property tax levy drops.

In Massachusetts, the administration has proposed allowing cites and towns to adopt a meals tax and a higher hotel/motel tax to relieve property taxes. However, Leslie Kirwan pointed out that tax relief is only one side of the equation. One cannot reduce reliance on the property tax without raising revenue from other sources or cutting costs. The Commonwealth is considering several cost-saving measures for municipalities, including allowing them to join the state’s Group Insurance Commission and to invest their pensions funds through the state pension pool.

The panelists proposed a number of alternative solutions to higher property taxes. Mary Clare Higgins pondered if one additional source of revenue might be to revoke the tax-exempt status of hospitals and schools, which are major sectors of the state’s economy. Piotti indicated that Maine is considering the idea of a statewide property tax with a homestead exemption for primary homes, to take advantage of revenues that could be raised from the large number of second homes in “Vacationland.” Sasse suggested that most states in New England have an opportunity to diversify their revenue sources, given that they rely less on charges and fees than states elsewhere.

Yet, as Sasse noted, in Rhode Island the property tax generates as much as the income tax and sales tax combined, and accounts for 98 percent of own-source local revenues in the state. Thus, it is likely to remain an important source of local revenues in the region. Given the stability of the property tax and the heavy reliance on it, part of the solution to taxpayer discontent may be to educate people about the importance of the tax in funding the services they rely on—and about how the tax works. Higgins reported that citizens’ misunderstanding about “poorly named” Proposition 2½ breeds discontent: citizens expect that their bills should not increase.
faster than 2½ percent annually. However, the law actually caps the total levy, not each individual bill, many of which have increased by significantly more than 2½ percent. This lack of transparency and understanding fuels voter discontent and makes it harder for local governments to raise revenues from the property tax.

**Question 3:** Are there particular factors, political or economic, that prevent adoption of local-option taxes in your state? Are there any special features about New England that suggest that local-option taxes are a viable alternative to property taxes, and should state governments impose a statewide rate on local-option taxes or give municipal governments the freedom to choose rates within a given range?

Several panelists reported that the sales tax rates of neighboring New England states, particularly New Hampshire—which lacks a sales tax—would make local-option sales taxes an exceedingly remote possibility. The panelists from Massachusetts discussed interest in and recent efforts to adopt local-option taxes, while the panelists from Maine and Rhode Island were not as warm to those ideas.

Higgins has been a proponent of local-option meal taxes for some time. Northampton’s tourists require additional city services, but at the present time, the only revenue benefit the city gets from visitors is from the parking meters. A local-option meals tax would allow the city to capture some of that revenue. Kirwan noted that the state of Massachusetts proposed allowing cities and towns to assess a 2 percent meals tax, and an additional 1 percent tax on existing hotel/motel taxes. However, she reported that the legislature seems concerned that local-option taxes do not help all communities equally and, as a result, it has not been in favor of them.

Piotti reported that local-option taxes have no political legs in Maine. There has been a concern that, by allowing a local-option tax, the state would “open the floodgates” and that “life would not be the same afterwards.” However, the state recently considered earmarking future growth in its sales tax revenue to communities in proportion to the volume of taxable sales generated within their borders.

According to Sasse, Rhode Island could not implement a local-option tax without first considering how the funds would be shared. Otherwise, such a move would introduce inequities into the tax system of that small state. He suggested that, rather than focusing on local-option taxes and their rate, states may want to consider ways to expand the sales tax base. This could provide more revenue, particularly if the base were expanded to cover the activities in the service economy, much of which is not currently subject to sales taxes.

**Question 4:** Do you believe that the type of state aid formula design proposed by Katharine Bradbury and Bo Zhao holds promise in your state?

The panelists were impressed by the proposed formula, including the two panelists from Massachusetts, upon which the formula was modeled. They agreed that formulas that address both capacity and need make sense. Piotti noted the importance of targeting state aid to the neediest communities, given limited revenues. However, the panelists did indicate that until states address their own structural budget challenges and fully fund state aid, the formula would remain academic in practice.

Ultimately, the formula would have to face some political factors in order to gain acceptance. An aid floor is used in the formula to ensure that every community gets at least some aid. But as Kirwan noted, having the aid floor is costly and detracts from the equalization objective. Higgins suggested that the aid floor is needed to recognize, to a certain degree, annual increases in the cost of providing local government services. Sasse commented that, outside the difficulty of funding the formula, the biggest problem will be getting consensus among local officials. Piotti noted that policymakers will make decisions based on how much money their own towns are going to get; people will want to see how they compare to other communities.

There is no one-size-fits-all solution to municipal finance challenges.
Kirwan concluded the panel discussion by noting that there is no one-size-fits-all solution to municipal finance challenges. Diversifying revenue sources available to municipalities, developing new ways to distribute state aid, and fostering state and local collaboration will all likely be needed to address this complex and entrenched issue.

**Concluding remarks**

In closing the conference, Robert Tannenwald, Vice President and Director of the New England Public Policy Center at the Federal Reserve Bank of Boston, noted that New England municipalities and state governments alike are clearly facing fiscal challenges. As speakers and panelists pointed out, the rising costs of health care and other public services are outpacing available revenues. With baby boomers retiring in the near future, increases in health care costs and a decline in the relative number of working-age taxpayers will further aggravate fiscal pressures.

This cautionary view highlights the urgency of state and local governments working together to study policy responses. While the fiscal challenges are formidable, possible policy solutions exist. However, they require creative thinking, thoughtful decisions, and most importantly, state-local collaboration. On the expenditure side, as the panelists noted, it is important and necessary for states and municipalities to work together on controlling costs, especially the rising costs of health care. To explore policy solutions on the revenue side, speakers also suggested changing state aid formulas to better target communities in greater need of assistance and exploring alternative local revenue sources such as local-option taxes. Because the proposed policy tools involve tradeoffs and there is no one-size-fits-all solution, state and local governments will need to work together to develop a diverse and robust set of policy options.
**Speakers**

**Richard F. Dye**  
Professor of Government and Public Affairs at the University of Illinois at Chicago, and Visiting Fellow at the Lincoln Institute of Land Policy in Cambridge, Massachusetts

**David L. Sjoquist**  
Professor of Economics and Director of Domestic Programs and of the Fiscal Research Center, Andrew Young School of Policy Studies at Georgia State University

**Bo Zhao**  
Senior Economist, New England Public Policy Center, Federal Reserve Bank of Boston

**Panelists**

**Andrew Reschovsky** (Moderator)  
Professor of Public Affairs and Applied Economics at the University of Wisconsin-Madison, and Visiting Fellow at the Lincoln Institute of Land Policy in Cambridge, Massachusetts.

**Mary Clare Higgins**  
Mayor, City of Northampton, Massachusetts, and President of the Massachusetts Municipal Association

**Leslie Kirwan**  
Secretary, Massachusetts Executive Office for Administration and Finance

**John Piotti**  
Maine State Representative and House Chair of Maine’s Joint Taxation Committee

**Gary Sasse**  
Executive Director, Rhode Island Public Expenditure Council (now Rhode Island’s Commissioner of Revenue)