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Policy Brief

# Population Growth and Local Government Finance: What Have We Learned?

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Between 1990 and 2000 South Carolina population increased by 15.1 percent, almost two full percentage points faster than the nation as a whole.[1] Some South Carolina counties experienced population growth rates that were more than double the state growth rate; some counties saw increases approaching 40 percent[2], creating a challenge for local government officials.

While population growth increases local government revenues, it also increases the demand for services provided by local government, such as public safety, road and street maintenance, and parks and recreation. There is concern among local officials in some communities that additional revenue generated by population growth will be insufficient to cover the increased expenditures required to provide services to the new residents. This concern led local officials in four communities – two counties and two municipalities – to hire researchers at Clemson University to analyze the impact of projected population growth on local government finances.[3]

Certain aspects of the fiscal impact of population growth are similar across communities. However, the results of the four studies also demonstrate that the net fiscal impact of population growth on local governments varies across communities. We suggest that differences in local development patterns and revenue sources account for much of the variation in fiscal impact across communities. While we need to be cautious about drawing conclusions from only four studies, we feel that we can draw some tentative conclusions about the fiscal impact of population growth on South Carolina local governments beyond these four communities.

## FISCAL IMPACTS ON COUNTY GOVERNMENTS

In the fiscal impact analyses we estimated the increases in county government expenditures and revenues associated with projected population growth for Lancaster and Jasper Counties. The estimated growth-related expenditures and revenues for the two counties are presented in Table 1.

**Table 1 - Estimated Growth-Related Expenditures and Revenues per New Household, Jasper and Lancaster Counties, South Carolina**

| | Lancaster County[a] | Jasper County[b] |
|---|---|---|
| **Capital Expenditures** | $1,463 | $2,460 |
| **Operating Expenditures** | 7,462 | 9,490 |
| **Total Expenditures** | 8,925 | 11,950 |
| **Revenues** | 7,266 | 29,082 |
| **Surplus/(Deficit)** | ($1,659) | $17,132 |

a – Ten-year present values
b – Twenty-year present values

Even if we account for the difference in the two studies' time horizons, population growth is clearly more beneficial for Jasper County than for Lancaster County. In Lancaster County, revenues are expected to mostly keep up with the increase in operating expenditures, but after accounting for growth-related capital expenditures we project a moderate deficit. In Jasper County, on the other hand, we expect that growth-related revenues will far exceed total growth-related expenditures. Part of the difference can be accounted for by the difference between the two counties' expected growth patterns. In Jasper County most of the population growth is expected to occur within its two municipalities, which will bear much of the burden of providing services to the new residents. In Lancaster County, most of the population growth has been occurring within the unincorporated part of the county, placing most of the service burden on Lancaster County government. However, we feel that the difference in growth patterns explains only a small portion of the difference. Table 2 presents a comparison of key characteristics of the two counties.

**Table 2 - Comparison of Lancaster and Jasper Counties, South Carolina**

| | Lancaster County | Jasper County |
|---|---|---|
| **Population (2000 Census)** | 61,351 | 20,678 |
| **Per capita assessed valuation (FY 2000)** | $3,487 | $2,884 |
| **Owner-occupied residential property (% of total assessed valuation)** | 22% | 18% |
| **Manufacturing property (% of total assessed valuation)** | 17% | 4% |
| **Commercial and rental property (% of total assessed valuation)** | 46% | 55% |
| **All other property (% of total assessed valuation)** | 15% | 23% |
| **Manufacturing employment (% of total employment)** | 26% | 7% |
| **Property tax rate** | 67 mills | 155 mills |

Sources: S.C. Department of Revenue; Bureau of Economic Analysis, Regional Economic Information System, U.S. Census Bureau; County Financial Statements.

An examination of the differences between the two counties provides a more complete, if tentative, explanation of the difference in fiscal impact. Lancaster County has a history as a manufacturing center. Consequently, Lancaster County has had a higher level of per capita assessed valuation, which has allowed it to tax property at a rate less than half that of Jasper County. Furthermore, manufacturing property typically generates more revenue than is needed to cover the expenditures required to provide it with public services[4], which also aids a county in maintaining a low property tax rate.

A local government's property tax rate affects its ability to respond to population growth. In South Carolina, local governments are heavily dependent on property tax revenue. For both counties we projected that property taxes would provide over 70 percent of growth-related revenue. Jasper County's higher millage rate makes its revenue system much more responsive to residential growth than Lancaster County's. Ironically, it appears that the counties that have experienced the lowest levels of industrialization and economic development in the past may be in a better fiscal position to respond to high rates of population growth in the future.

## FISCAL IMPACTS ON MUNICIPAL GOVERNMENTS

The Jasper County study included fiscal impact analyses of the City of Hardeeville and the Town of Ridgeland, the two municipalities in Jasper County. The estimated growth-related expenditures and revenues for the two counties are presented in Table 3.

**Table 3 - Estimated Growth-related Expenditures and Revenues per New Household, Base Scenario, Hardeeville and Ridgeland, South Carolina**

| | Hardeeville[a] | Ridgeland[a] |
|---|---|---|
| **Capital Expenditures** | $6,918 | $6,114 |
| **Operating Expenditures** | 35,273 | 27,360 |
| **Total Expenditures** | **42,191** | **33,473** |
| **Revenues** | **38,033** | **30,222** |
| **Surplus/(Deficit)** | **($4,158)** | **($3,251)** |

a – Twenty-year present values; assumes average residence value of $180,000

The greater per household expenditures presented in Table 3 reflect the municipalities' more intensive level of public service provision relative to counties. However, municipalities also collect greater per household revenue than do counties. This difference in revenue is largely a result of the greater level of commercial development that accompanies the higher population densities that exist in the incorporated areas. For both municipalities, population growth is expected to generate sufficient revenue to cover increases in operating costs, but paying for growth-related capital requirements results in a net deficit. In an alternate scenario, with higher average residence value, both municipalities are projected to experience a net surplus. The projected growth-related expenditures and revenues for the alternate scenario are presented in Table 4.

**Table 4 - Estimated Growth-related Expenditures and Revenues per New Household, Alternate Scenario, Hardeeville and Ridgeland, South Carolina**

| | Hardeeville[a] | Ridgeland[a] |
|---|---|---|
| **Capital Expenditures** | $6,918 | $6,114 |
| **Operating Expenditures** | 35,273 | 27,360 |
| **Total Expenditures** | **42,191** | **33,473** |
| **Revenues** | **44,829** | **34,378** |
| **Surplus/(Deficit)** | **$2,638** | **$905** |

a – Twenty-year present values; assumes average residence value of $240,000

While higher residence values are expected to produce a net fiscal surplus for both communities, the resulting improvement in Hardeeville's fiscal condition is much greater than Ridgeland's. Table 5 provides a comparison of key characteristics that helps to explain the difference in the two communities' fiscal responses to population growth.

**Table 5 - Comparison of Hardeeville and Ridgeland, South Carolina**

| | Hardeeville | Ridgeland |
|---|---|---|
| **Population (2000 Census)** | 1,793 | 2,518 |
| **Gross Retail Sales (FY 2001)** | $39,134,000 | $60,936,000 |
| **Property Tax Revenue (as % of general revenues)** | 28% | 14% |
| **Local Option Sales Tax Revenue (as % of general revenues)** | 11% | 26% |
| **Accommodations Tax Revenue (as % of general revenues)** | 25% | 16% |
| **Other Revenue (as % of general revenues)** | 36% | 44% |
| **Property tax rate** | 147 mills | 105 mills |

Sources: S.C. Department of Revenue; U.S. Census Bureau; Municipal Financial Statements.

Both Hardeeville and Ridgeland are located along Interstate 95 and have a large level of retail activity for communities of their size. Ridgeland, however, has historically had greater retail activity than Hardeeville and consequently relies much more heavily on local option sales tax revenue. As a result, Ridgeland has a property tax rate that is about two-thirds of Hardeeville's, is much less reliant on property tax revenue, and has a fiscal system that responds differently to population growth than Hardeeville's.

## CONCLUSIONS AND IMPLICATIONS

Several conclusions can be drawn from this analysis. First, local governments appear to have fiscal systems that generate approximately enough revenue to cover the increased operating expenditures associated with population growth. However, the growth-related capital expenditure deficit leaves communities with three choices: (1) reduce the level of public services they provide, (2) increase existing tax rates, or (3) find new sources of revenue. The communities we have worked with have pursued the third option. South Carolina state law allows local governments to impose development impact fees to recover growth-related infrastructure costs. However, to date no county has imposed impact fees under the terms of the impact fee statute. Local officials from around the state give two reasons for not imposing statutory impact fees: The law is excessively cumbersome to administer and it produces impact fees that are insufficient to cover the costs of infrastructure.[5] As a result, the communities we have worked with have used a number of methods to encourage developers to enter into voluntary development agreements under which they make cash or in-kind contributions to offset the cost of growth-related capital improvements.

Second, it appears that historical development patterns affect a community's selection of revenue sources, which in turn affects their ability to pay for growth-related expenditures. Consequently, communities which are already fairly industrialized and urbanized may have fiscal systems that are the least able to generate the revenue needed to keep pace with population growth.

Third, the heavy reliance of local governments on property tax revenues may lead communities to discourage the construction of lower-valued housing, because it is unlikely to generate sufficient revenue to provide residents with public services. This situation has obvious implications for the continued existence of affordable housing in rapidly developing communities.

Finally, because local governments depend so heavily on property tax revenues, state officials should be careful in implementing property tax reform. The South Carolina legislature is currently considering a proposal in which local governments would give up property tax revenues in return for a share of revenue produced by a two-cent increase in the state sales tax rate.[6] While most local officials appear to be apprehensive about the proposal, those in fast-growing areas should be especially so. A shift from property to sales taxes may degrade their ability to respond to the fiscal demands of population growth.

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## NOTES

[1] National Atlas. n.d. Population Change and Distribution: 1990 to 2000. <http://nationalatlas.gov/articles/people/a_popchange.html>.

[2] S.C. Office of Research and Statistics. n.d. Comparison of 1990 and 2000 Population and Percent Change. <http://www.ors2.state.sc.us/census2000/1990_2000_County_Compare.htm>.

[3] The four fiscal impact studies are contained in two reports: William E. Molnar and Charles Taylor, *Residential Fiscal Impact Assessment, Lancaster County, South Carolina* (Clemson, SC: Clemson University, January 2005) and Charles Taylor and William E. Molnar, *Fiscal Impact Assessment, Jasper County, City of Hardeeville, and Town of Ridgeland, South Carolina* (Clemson, SC: Clemson University, January 2006). The reports are available for download at <http://www.strom.clemson.edu/publications/taylor/lancaster.pdf> and <http://www.strom.clemson.edu/publications/taylor/jasper-fia.pdf>.

[4] See, for example, Jeffrey H. Dorfman, et al., *The Economic Costs of Development for Local Governments* (Athens, GA: University of Georgia, January 2002) <http://www.forestry.uga.edu/h/centers/cfb/files/EcCost.pdf>.

[5] John O'Connor. 2005, July 4. "Impact fee proposal is losing its appeal." *The State (Columbia, SC)*, p. A1.

[6] Tim Smith. February 9, 2006. "House OKs Tax-Shift Plan." GreenvilleOnline.com, <http://greenvilleonline.com/apps/pbcs.dll/article?AID=/20060209/NEWS03/602090307>.