



Fiscal Impact Analysis: Evolution and State of the Art

By Dr. Mason Gaffney

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FISCAL IMPACT ANALYSIS: EVOLUTION AND STATE OF THE ART

by Mason Gaffney

In almost every management field we find packaged computer models being introduced. Most of these are old wine in new bottles. While the new bottles are potentially better than the old, they also hold potential for more damage and misuse through lack of understanding.

They are, on the good side, more systematic and interactive, capable of handling many variables dynamically, replacing the old "inextricably interwoven" cliché with functional relationships. When abused, they become just another communication barrier, another mystery wherewith to befuddle the uninitiated, with obvious appeal for charlatans, wizards and humbugs, as well as for authoritarians welcoming another tool of I&O (Intimidation and Obfuscation.)

The user's problem is that the causal assumptions, the coefficients, the lags, even many of the goals are embedded in the program in ways he cannot evaluate without replicating the work himself. The user may also be unaware of several important factors which models cannot handle any better than he, because the quantitative importance is unknown and/or judgmental. Synergistic effects of growth, for example, are generally unknown. Trade-offs among conflicting goals and interest groups are often judgmental.

Model users therefore need an independent evaluation of models, to prevent abuses. This quality control will help the industry, too, by raising overall user confidence. As part of this evaluation, we present

here a synoptic view of why Fiscal Impact Budgeting System models are used, and in what context they should be evaluated.

I. Animus

The animus behind fiscal impact analysis is the suspicion that the net impact of a proposed growth impulse, program or strategy may be negative; and that the benefits and costs to the community are so evenly balanced, and so interwoven, that a very careful accounting is required to help arrive at a decision or policy. Gut-level confrontations between developmentalists and environmentalists, each stressing a small package of arguments weighted one way or the other, are increasingly perceived as sterile and counterproductive. Conventional economic analysis and public finance doctrines are perceived as being addressed to another public than the local government, and therefore not entirely relevant.

Models respond to the fact that there are many pluses and minuses to sum up and net out before reaching the final net impact; and also to the fact that local economy and land use are interactive systems that require systems analysis. While they do not comprehend the less known and less quantifiable dimensions of synergism or holism, they do take a first step by incorporating concepts of base multipliers and input-output analysis.

Another problem is the proliferation of complex intergovernmental transfers both on the granting and taxing sides, based on formulae which, in their overall impact, are exceedingly complex to trace through. Some state and federal "grants" take the form of public works, financed and built in advance and therefore not conditional on responsive growth. These need one sort of treatment. Others are based on population, in whole or

part. Yet others are mandated local expenditures, generally people-related, and uncontrollable save in advance of allowing immigration. Then there are state and federal taxes, mostly people-related, which to the locality are, in the Marshallian sense, "onerous." Net fiscal impact is the bottom line of a very tedious journey through all of these with their interactions. The fact that the public works are often given free and in advance creates a strong presumption that the balance of later impacts may be negative.

✓ A growing concern is with the spatial layout of growth. Energy-guzzling sprawl patterns look increasingly costly when the newly-multiplied private costs are added to the public infrastructure costs, and the new emphasis in planning literature is strongly anti-sprawl (Real Estate Research Corporation, 1974; State of California, Office of Planning and Research, 1977; Downing, 1977). City centers and central cities are increasingly reacting to feelings of exploitation by suburban and peripheral growth, and asking for analytical confirmation and quantification. Analyses of utility rate structures are questioning the efficiency as well as the equity rationale of promotional declining block-rate structures, with their exploitation of central cities by suburbs, and residences by industries (Musial, 1972).

Another, and often subliminal animus behind impact studies is the need for a socially more legitimate surrogate for ethnic and class feelings which are not culturally acceptable to express directly. Or it may be a feeling against unloved federal mandates like busing, regardless of ethnic feelings, which come in tandem with ethnic issues.

Another animus is opposition to pollution which is related to growth, and aggravated by some patterns of growth vs. others. Pollution factors should be more amenable than ethnic feelings to being modeled.

II. Limits on an Earlier Burgeoning of Fiscal Impact Analysis

It is curious that as basic a question as fiscal impact analysis has such a short history. No doubt if we scoured history we would find precedents, but the historical antigrowth position of mercantilist cities has been more based on market power, both as seller of goods, and employer and buyer. The German historical school, exemplified by Schmoller, has long since consolidated this thesis. In the United States the oligopsonistic behavior of small city employers seeking to avoid spoiling the labor market by admitting new industrial employers is a well known phenomenon. With such strong forces presiding over growth control, there was little need for fiscal impact analysis. Only in modern times with the regional and national equalization of wage rates, and the growing relative importance of taxation, has this all changed.

More powerful, too, in the United States has been the frontier growth doctrine, with new cities continually being founded, and competing for routes and markets and growth. While some restrictive cities might stagnate, others picked up their rejects and worshipped growth. It was the route to prosperity for land speculators, and at the same time a safety valve for the discontent rising from the problems of maldistribution of wealth in the older and stagnant cities. Frontier growth was also the despair of radical activists and organizers, whose human material was progressively coopted and de-radicalized. It dampened much of the demand for a redistribution of wealth through the tax system -- a demand which

today inspires much of the defensive posture of localities asking for fiscal impact studies.

After World War II urban growth met little questioning, in part because of the heritage of "dead land", tax-reverted land left over from the depression, land already divided into small parcels and supplied with street improvements. Demand for this land was welcomed unequivocally, both by counties which had foreclosed on it, or by banks in the same predicament (Aschman, 1949). Planners like Gulick and Blucher had opposed selling the land just to "get it back on the tax rolls" until demand increased, at which time this was perceived as on balance advantageous.

The "objective function" of city policy was seen to be enhancing real estate values (Weimer and Hoyt, 1948 and later editions). For many years following World War II, analytical advances served this growth orientation and the implicit acceptance of maximizing land values as the bottom line of policy. *This was the period when economic base analysis was in flower.*

The line derived from native, business-oriented Homer Hoyt merged effortlessly with another one derived from Keynesian international trade theory. Export industries which brought in outside money were "basic", and had a "multiplier" effect on the dependent local or "filler" industries, the market-oriented camp-followers. Charles Tiebout and Charles Leven articulated this position in a sophisticated way. While they themselves were not guilty, some enthusiastic proponents were prone to think in infant industry terms. The difference between regional and national infant industry thinking is that the region or city cannot block imports to protect

local industry; so instead it encourages export industries, to improve its regional balance of payments. Regional accounting was developed, with leadership from Werner Hochwald and the St. Louis School. Regional Economics under Walter Isard became a recognized discipline, incorporating input-output analysis into models of regional growth, giving greater specificity to concepts of economic base and multiplier.

In this growth-oriented era, Malthus was dead. Resource limits had no credibility. Declining areas were considered tragic, and the Area Redevelopment Administration with the pen of Victor Roterus was funded to redress their losses. Federal public works' and contracting agencies sponsored studies of benefit/cost analysis in which secondary benefits loomed large (secondary benefits, external pecuniary economies, and base multipliers are all close cousins). The Federal Inter-agency River Basin Committee sought to bring some order to this with its 1950 "Green Book" on Benefits and Costs, but in practice secondary benefits carried the day and the only effective constraint on public works and contracts was the overall budget. N.A.S.A. was particularly conspicuous in its funding of local economic base studies; but expanding public universities in the soaring sixties were no less zealous to analyze their community impacts. It is significant for later developments that *none of these public agencies would fare as well under fiscal analysis*, being tax exempt. Highway impact studies were as plentiful as alley cats, and they included usually a study of land value impacts, always positive and large. (Chicago Area Transportation Study; Bay Area Transportation Study; Southeast Wisconsin Regional Planning Commission, highway studies; CALIFORNIA HIGHWAYS, a free monthly publication of the California Department of Highways.)

The pro-growth mindset had many components. Widening the market to achieve economies of scale and synergy was prominent. Urban magnetism was highly prized. Older areas were to be cleared out so they might be renewed and replatted, eliminating obsolescence and bad housing. Regional increasing returns were recognized, exemplified by the movement of market-oriented industry and headquarters to California, which by growing had escaped from its previous colonial status and become the El Dorado its discoverers once sought. In diversity there was stability, too, and security from monopsonistic employers in small company towns. Governments, too, were thought to enjoy economics of scale. Distributional and allocational rivalries were to be reduced to the level of needless squabbles, with growth creating abundance for all. Increased population brought more voting strength, and more government contracts and works. There would be more matching grants, more magnetism for transportation routes. Early development would stifle and abort potential rivals, which might become your colonies. Land would be turned to higher and higher uses, transmuting base values into gold. The growing city and region contributed more than others to victory in the international growth race against foreign nations. Finally, any interference was in violation of the rights of private land-owners to develop *their* land.

In all that, there was little heed to governmental motives. Margolis observed in 1968, "Benefit-cost studies took as their point of departure the welfare of the nation and they paid little heed to the peculiar problems of the government." Local government would go along with growth because what is good for one is good for all. Growth-oriented governors and legislatures first gave public works to localities, and finally thrust them upon localities, confident of cooperation.

There was, to be sure, a latent anxiety that a new overhang of premature subdivision could develop, as in the late twenties. But this was abated by tract housing development, where developers synchronized streets with houses; and by state-federal financing of other infrastructure, financed by income taxes which spared much burden to property owners -- indeed, made much property a tax shelter -- extending the holding power of owners far beyond previous experience. It was widely anticipated that the local property tax would wither away altogether.

The impact of public works on land use and local finances was badly neglected in scholarly literature, which became fragmented and compartmentalized in this period. Transportation and highway economics were one thing; land economics another. The former Journal of Land and Public Utility Economics became simply Land Economics. There were efforts (Mitchell and Rapkin, Wingo; 1961; and Gaffney, 1960) to integrate transportation economics with land use, and to analyze subsidies and diseconomies in transportation. The dominant thought, however, held that transportation institutions were substantially neutral and that land use choices therefore represented free expressions of consumer tastes (Meyer, Kain & Wohl, 1966).

III. Disenchantment with the Fiscal Impacts of Growth

There were long a few worms in the apple of growthmanship. An early foreboding was the definitive zoning case of *Euclid v. Ambler*, 1926, wherein *Euclid* was allowed to zone land for a purpose clearly exclusionary. By 1950, the planning literature was beginning to attack the "Fiscal Approach to Land Use Planning." Snob zoning was generally decried and viewed as a

threat to good planning and social justice, with little sympathy (in the literature) for the problems and motives of its growing votaries. Tiebout, generally a growthman, did not perceive this weak movement as a threat, but rationalized it.

Another foreboding was the behavior of cities disposing of cleared land under the Federal Urban Renewal Program. Rather than sell to the highest bidder, many cities (if they sold at all) selected rather the bidder who promised to invest most in buildings (hence pay the most taxes). Fiscal impacts took precedence over market signals.

Other forebodings came from veteran Homer Hoyt, an elder statesman of economic base multiplier analysis. In his 1951 study of Arlington County, Va., Hoyt laid out the land use requirements of anticipated growth, and hence the expenditures required to serve them. Here, base analysis coupled with land economics was used not to promote growth but to predict public costs. The result was rather a dimmer view of growth than before. Hoyt became known as a critic of apartments and other fiscal deficit generators. Likewise, Walter Isard and Robert Coughlin (1957) also began to raise questions about the benefits of growth.

In 1956 Maryland passed the first law mandating preferential assessment of farmland, and California followed in 1957. The impact of these public works' extensions on land values was being noticed by assessors, and some holders of ripening land were objecting to being carried along unwillingly -- and were getting public support.

Meantime, a number of changes were in process in intergovernmental relations which changed attitudes a good deal. Federal and state income taxes rose to very high levels, along with payroll taxes, and drew heavily

on wage and salary incomes, leaving that much less to contribute to local government. Federal agencies, with their own inner inertia, were more and more committed to spending on public works, regardless of local demands. The property tax, thought to be dying, rose from the ashes and began taking a large bite. This gave many owners second thoughts about the goal of high real estate values as the "objective function," as assumed in the pro-growth syndrome. Increasingly, real estate owners viewed rising values more as a curse than a blessing, because of higher tax liabilities. The result may seem ludicrous to an economist, but has lent enormous strength to taxpayer revolts.

Schooling and welfare and socialized medical costs, all people-related, have escalated. Much of the spending is mandated. The organic theory of government has shifted from the local to the state level, leaving local government based on the contract theory of government, but feeling overborne by organic (redistributive) mandates imposed by the state. The result is more and more to oppose immigration. Many city residents feel bruised and battered by state government which responds less to them and more to farmers, suburbanites, and propertyless groups in the cities (but not of them).

Another big change is environmental. Resource scarcity and the age of limits is a new theme, arguing against growth. It merges and supports local environmentalism. Growth brings pollution and lowers the quality of life. Amenities are tax-free, and not to be lightly relinquished.

Then there are massive sociological changes. When restrictive covenants were declared unenforceable by the courts, zoning found a new role, to screen out minorities as well as the poor. Ethnic feeling is involved,

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and also a desire to exclude organized or organizable groups thought to have redistributive designs and voting patterns. Banfield and Wilson (1964) have shown that "non-homeowners show more taste for public expenditures that are to be financed from property taxes than do homeowners." The message to suburban homeowners is loud and clear.

The local fiscal impact of lower-wealth immigrants would be softened by shifting educational finance to the state level, the logical seat of sovereignty and therefore of the organic concept of the state. Several state courts have said as much; but few state legislatures have responded as directed, and the U.S. Supreme Court in Rodriguez has thrown the ball back to these very legislatures. At the same time, this same court has continued to reaffirm the rights of localities to use zoning as they see fit. Dean Charles Meyers, Stanford Law School, opines that the Court has taken a very strong position in *Warth v. Seldin* 422 U.S. 490 (1975), invoking standing requirements to avoid reviewing one case. Only landowners have standing, and their subservience to the police power, without claim of compensation, has been consistently upheld for fifty years (Meyers, 1977, Ellickson, 1977).

A related issue is busing, whose unpopularity needs no documentation. Taxpayer rebellion in California under the Jarvis-Gann initiative would have the effect of weakening the public schools, and it is entirely possible that this is an indirect reaction to busing.

Another factor is the growing reaction to interjurisdictional exploitation. Cities and city centers especially have been exploited by suburbs and fringe areas, and are seeking to impose more costs to growth directly

on the growth areas. There is growing support for "reaches" pricing, which charges each customer with his percentage of the line that reaches him. Early students like Isard and Coughlin were indifferent to density and settlement patterns, seeing no systematic cost differences; more recent research may be changing this emphasis.

Scholarly support for these tendencies is the user-charge literature, a logical application of micro price theory to municipal services. The Chicago School has been prominent, but not alone in this work. Hirshleifer, Milliman and De Haven, in WATER SUPPLY, made the case for user charges. Dick Netzer has advocated replacing the property tax on buildings (not land) with a "family of user charges," finding the value of buildings to be unrelated to service costs imposed on localities. Donald Shoup has written on the "Lakewood Plan" of L.A. County for contracting specific services to local governments.

It is but a step from user charges to the benefit theory of taxation. Jerome Milliman, Mason Gaffney, and Julius Margolis, along with many others, have pointed to the desirability of recouping public works' spending from taxes assessed against the resulting increments to land values.

The safety valve rationale for growth has died with the growth of low density zoning, and the awareness that urban frontiers offer more to capital than to labor. Radical activists oppose new settlement patterns that make it harder to organize the "masses"; and find many sweet victories in fighting evictions for highway extensions in inner cities, victories where they join forces with environmentalists, their sometime opponents. Highways have become increasingly unpopular, compared with the glory days of the 1950-70 explosion.

Central cities, left with more than their share of the poor and the radical, are increasingly alarmed at the fiscal impact of rent controls and abandoned real estate and dropping values. Public housing and other tax-exempt real estate hits them hard; anti-eviction campaigns are a threat.

Large episodes of recession in the heavily capital-importing regions, notably southern California, have taken some of the bloom off base multipliers and El Dorado effects. Stability is now more sought after. It is recognized that rapid growth means an economic base which is, temporarily at least, composed in large part of outgoing promissory notes, posing dangers of negative multipliers in the future.

Hans Blumenfeld and others, meantime, have demolished much of the base multiplier mystique. Perhaps they overkilled it because, with all its faults, it served in lieu of a theory of synergy. Regardless, hard-headed municipal finance officers will require something more in the future.

IV. The Selective Growth Management Movement

These years of sobering have brought us to the movement for selective growth management. For a few suburbs, this is old hat. The wealthiest of them have practised it for several decades. What is new is the wildfire spread, as from San Mateo County to Santa Clara County, a few miles in space, but light years in time. Everyone now wants to test the fiscal impact of new growth.

Moreover, the new prudence has moved even to the state level (the traditional seat of booster programs). Florida and Oregon are telling visitors to enjoy and go home. Vermont is taxing absentee speculators,

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defining them essentially as outside builders. Regional agencies, too, are retrenching. The Washington Sanitary and Sewer Commission case is well known. The Association of Bay Area Governments is using its limited leverage over federal grant allocations to enforce a red line growth perimeter.

Cities are no longer run simply with revenue forecasting: expenditure forecasting is required, too, and especially where there is new growth. Taxpayer revolts are in the air; no longer can developers blithely assume they will receive subsidies from central cities anxious to increase their trade territories and economic base. No longer can civil engineers be used as fatherly authoritarian figures rationalizing "required" expenditures for public works: the public perceives them now also in terms of monument builders and gold platers.

Scholarly response to this new movement is lagging. The closest analogy is perhaps Gilbert Tucker's old THE SELF SUPPORTING CITY, but that was more concerned with selling the single tax and was so perceived. Steven Cord, editor of INCENTIVE TAXATION, occupies a similar role today. There were several works in the sixties that seemed relevant, but they had an Olympian quality, being addressed to all mankind rather than to the finance officers of city governments. These included Chinitz and Tiebout (1964), Lichfield (1960), and Isard and Coughlin (1957). Exceptions were Homer Hoyt and John Dyckman, with their consulting experience, but they wrote before the great environmental changes that brought us to our present pass.

As to distributive questions, scholars tended to treat these in the national manner, even when writing of local matters, so the spirit is leveling -- not what municipal managers and their local real estate clients

are looking for. Scholars wrote of "public goods", but failed to ask. "Which public?" To some degree the Public Choice school has moved into this vacuum, led by James Buchanan, but more in a philosophical than an operational way. An exception was the effort of Craig Stubblebine and Ron Teeple to work out a response to the Serrano mandate in California, but both the response and the mandate have been abortive.

In 1948, Weimer and Hoyt could take the maximization of real estate values as the obvious goal of local policy. Now, this mission accomplished, the emphasis has shifted more to conserving the gains made, and sheltering them from bleeding by immigration and radical activism and redistributive taxation. While economists have lagged in perceiving this change, legal scholars have led, and been extremely sensitive. Coons and Sugarman, of course, in their several works on school finance, have provided the groundwork for Serrano and its implementation. Don Hagman has popularized the concept of "Windfalls for Wipeouts" and the need for more equity (although only among landowners). The movement for Transferable Development Rights is one approach to meeting the Hagman problem. Robert Ellickson, Ira Michael Heyman, Daniel Fesler, and Charles Meyers have all, in one degree or another, viewed with alarm the fiscal mercantilism movement; and activist courts have taken a lead in weakening at least some aspects of it.

These legal scholars thus were not in tune with the current desires of municipal finance officers. *The recent spate of fiscal impact studies has come, therefore, from the cities themselves, their consultants, and a few presuent scholars.**

*These include such works as the Management and Control of Growth published by the Urban Land Institute in 1975 which includes chapters by Thomas Muller, "Fiscal Impact: Methods and Issues;" Ashley Economic Services, "The Fiscal Impact of Urban Growth;" and a piece by Gruen Gruen and Associates entitled "The Impacts of Growth." Also, see (Meyer, Kain and Wohl, 1966; Bahl, 1969; Wilensky, 1970; Muller, 1974; Bahl and Gustely, 1974; and McMullin and Bryant, 1976)

blunders, solenism, etc.

VIII. APPENDICES

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APPENDIX A

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*to these statements are
a bit too strong - call me
at 213 8251324 if you want a better feeling for the issue*

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*How about
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