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City budgets slammed by falling property taxes

By Tami Luhby, senior writer

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NEW YORK (CNNMoney.com) -- The housing crisis is finally catching up with cities -- and the impact isn't going to be pretty.

Property tax revenues started to decline in 2010 after years of growth, according to a report released by the National League of Cities on Wednesday. Cities expect property tax revenues to fall by 1.8% in 2010, after rising by 4.2% in 2009.

This drop lagged the housing market collapse because property tax bills are based on assessments, which are slow to adjust to market value changes.

But the worst is yet to come, according to the league's report. The full brunt of the housing bust won't be felt until 2011 and 2012 as more property values are reassessed. And commercial real estate values may dive in 2012, exacerbating the problem.

"Cities are now in the eye of the storm," said Christopher Hoene, the center's director for research and innovation. "The pain is intensifying."

Though income taxes are expected to rise 1.8% this year, relatively few cities have income levies. Instead, sales and property taxes dominate their revenue streams. And that means a double whammy: Sales taxes are budgeted to drop 5% in 2010.

Overall, the league projects a 3.2% decline in cities revenues in 2010 -- the largest downturn in the report's 25-year history. It is also the fourth year in a row that total revenues have dropped.

Cities are in the worst shape they've been in since the Great Depression, said the report's co-author, Michael A. Pagano, dean of the College of Urban Planning and Public Affairs at the University of Illinois at Chicago.

This means cities must continue to slash services and shed personnel, with expenditures projected to fall by 2.3% this year. That's a tie for the largest cutback ever; cities have only cut back on spending five times in the past quarter-century.

Nearly 8 in 10 cities are expected to eliminate staff in 2010 -- for a total of 480,000 jobs lost -- on top of the 67% of cities that handed out pink slips last year.

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Nearly 75% of cities are instituting hiring freezes; 54% are mandating salary reduction or freeze; and 22% are requiring furloughs.

Some 17% have cut health care coverage while another 7% have trimmed pension costs, though these are harder to do.

Some 69% of municipalities are delaying or canceling capital projects, while 34% are modifying health benefits.

A quarter of cities are cutting public safety, which is usually among the last areas cities like to touch. A year ago, only 14% were slashing spending on public safety.

Riverside, Calif., for instance, has reduced its budget to $190 million, from $228 million, over the past three years, said Mayor Ron Loveridge, the league's president. It has cut its staff to 2,000, from 2,500, mainly through attrition.

The city also has reduced library and community center hours in recent years, and the police department has lowered the number of officers on patrol and devoted fewer resources to certain programs, such as gangs.

"But we've balanced our budget because we have to," he said.

Cities are also trying to fill their coffers by hiking fees and taxes. Some 40% of cities raised fees, while 23% upped their property tax rates. Another 23% increased the number of fees they charge.

But it's not easy for elected officials to boost taxes and fees in the midst of a recession, Loveridge said.

And the outlook for 2011? Gloomy. Eight in 10 city finances officers say they'll be less able to meet their fiscal needs in 2011 than they were this year.

Cities are also bracing for the end of federal stimulus money next year, which could also mean cuts in state aid since Recovery Act funds have been propping up state budgets as well.

Municipal officials are not expecting much to be done in Congress until after the November elections, but they are anxiously awaiting federal lawmakers' decisions on appropriations, state grants, transportation and infrastructure funding, and unemployment insurance -- all of which will have an impact on their budgets.

"Even if the economy turns around tomorrow, cities won't feel it for two to three years," Pagano said.

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