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Fiscal Impacts of Large Developments On Small Communities

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Large scale development projects in agriculture, mining, lumber and hydropower generation have quite literally changed the face of the state of Idaho. Examples include irrigation projects, food processing plants, metals and potash mining, wood products manufacturing and the Dworshak dam. Such projects have played a major role in attracting immigrants to the state and redistributing the population within its borders. They have also helped attract other types of industries, thereby broadening the economic base and helping foster economic growth.

Characteristics of Large Scale Developments

Large scale projects are defined as those that profoundly change the social, economic and environmental character of an area. Such projects commonly create employment in excess of that which the local labor market can provide. This results in large in-migration and rapid growth. Conversely, when large scale firms reduce or stop their activities, the impacts on the community and area are profound also. The Bunker Hill mine closing in Kellogg and various lumber and wood products plant cutbacks and closures (most recently the Potlatch lumber mill in Lewiston) demonstrate the impacts of large scale retrenchment.

Large scale development projects are undertaken because (1) a demand exists for the product or products to be produced; this demand is most likely national or international in scope, and (2) the site selected for the complex has a production and/or distribution cost advantage over alternative locations. General Motors selection of Spring Hill, Tennessee, for its Saturn auto plant demonstrates these two factors.

When a plant cuts back or stops production, it is again for one or the other (or both) of the same basic reasons: product demand has dropped and/or the plant's costs are higher than those of other sources of the product (domestic or foreign).

Large scale development projects, then, come and sometimes go because of one factor — demand — over which the community has no control. National and international product demands are determined primarily by the business cycle in the short run and by changing consumer preferences and product development over longer time periods.

The other factor — the cost of production/distribution — may be partially controllable by the community. Labor cost, the single largest cost component of most manufacturing/processing activities, may be influenced by local action. Renegotiation of labor contracts is one method of achieving lower costs. Other production/distribution costs, however, are beyond control of the community: interest rates (again determined by the business cycle), raw material availability (an ore vein becomes depleted) and location (changing transportation modes and markets).

Over time, plants, companies and even industries come into communities. They often prosper, sometimes languish and even depart. The communities in which they locate prosper and languish as well, but they seldom depart, at least not for years or generations after their economic base has been lost.

The question that citizens, public officials and students of community development face is how can communities, many of them one-industry or one-company towns, cope with the changes brought about by both the construction and operation and the decline or departure of large scale development projects? This is a vital question for Idaho and other western states whose economies depend on the demand for natural resources. However, the details of national and international market demands — when, how much and at what price — are uncertain. But just as surely as the energy, metals and lumber markets are now in the doldrums, they will again become active and again fluctuate in their levels of activity. Meanwhile, the "permanent" population and the community infrastructure (schools, churches, local units of government) must seek to adjust to changing numbers of school age children, housing requirements, welfare needs and levels of police and fire protection.

In a market-oriented or capitalist economy many, probably most, adjustments to economic change are made by the "private sector" — individuals, families and firms. The private sector, however, must be complemented by a "public sector" to provide and maintain a basic education system, streets and roads, law enforcement and other services for the common good.

Earlier research has shown that municipal governments in rural Idaho have found ways of covering the costs incurred by their cities from individual small scale developments (shopping malls, residential subdivisions, condominiums, apartment complexes).[1] But these projects have little or no impact on employment, in-migration or school enrollment. Large scale developments are a different story.

While large scale projects have many direct and indirect benefits for local jurisdictions, they also have their costs. The influx of new residents attracted by a project creates additional demands for publicly supplied services. New and improved schools, roads, water and sewer facilities, police and fire protection and waste disposal sites are often required to cope with the induced increases in demand.

In addition to these new demands, the rapid and unplanned growth associated with large developments comes with its own special set of problems or "impacts." These fiscal impacts present a challenge to local jurisdictions in Idaho. Furthermore, and of particular importance when the economy is not expanding, they may also work in the reverse direction.

Types of Fiscal Impacts

Fiscal impacts of growth fall into four broad categories: spillover impacts, front end deficits, "boomtown" effects and uncertainty impacts.

Spillover impacts are those impacts associated with large scale projects that "spill over" the boundaries of the jurisdictions in which they are located. Since projects are frequently located across state, county or school district boundaries from the areas they impact, these jurisdictions may not be in a position to benefit from new tax revenues that the projects generate. This is particularly evident in Idaho where much of the local revenue is derived through property taxes. Thus, the costs of a project spill over the boundary and are not offset by increased revenues.

Front end deficits are another type of fiscal impact associated with large scale projects. Public sector costs often begin to mount nearly as soon as the project is conceived. Revenues, on the other hand, do not begin to flow until much later in the life of the project. Jurisdictions frequently suffer a tremendous increase in front end costs, unmatched by revenues, early in the life of a project.

"Boomtown" effects result when developments induce rapid and unplanned growth in small towns and the markets for labor, housing and public services are quickly overwhelmed. This creates a number of complex and interacting fiscal problems that have been observed and described in large scale development projects.

Uncertainty impacts have important effects on fiscal decision making. The uncertainty associated with project completion, the date of completion, the scale of the project and the ultimate duration of the project create an extremely difficult planning atmosphere. Uncertainty influences the decision of jurisdictions to provide services, banks to provide capital and individuals to make investment decisions. Although not readily quantifiable, the fiscal impacts of uncertainty cannot be overemphasized.

The possibility that a project will not be completed is a very real danger in today's volatile economy. Large and abrupt price swings in a project's product or its inputs may cause the termination of the project. The size or complexity of a project is no indicator of the possibility of completion. The EXXON oil shale project in Parachute, Colorado, which was indefinitely suspended before operations began, is an extreme example of this effect. In Idaho, the Cyprus molybdenum mine in Challis has not been developed to the scale originally envisaged.

The fiscal effects of project termination are quite clear. Jurisdictions have often made huge capital outlays with little or no hope of cost recovery. In Idaho, there is little legal recourse open to local jurisdictions if there are no previous contractual agreements.

In the face of unfavorable price swings, many companies will elect to delay the date of project com-

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[1]Initial and Long-Term Fiscal Impacts of Developments on Rural Municipal Governments, by Don Blayney, Stephen M. Smith and Gerald Marousek, Univ. of Idaho Ag. Exp. Sta. Res. Bul. 123, March 1982.

pletion or production. This too will affect local jurisdictions since it will delay the arrival of expected new employees, secondary businesses and industry. Although the supporting infrastructure may be in place and the fiscal costs incurred, the projected revenues may not be forthcoming. This can place local jurisdictions in a potential deficit situation.

Alteration of the planned scale of a project may also affect fiscal planning. If public services sufficient for 5,000 new residents are put in place, but only 2,500 new residents ultimately arrive because of a scaledown of operations, considerable excess costs will have been incurred. Revenue projections may not be met, and the local jurisdictions may be placed in a fiscal bind. Again, the Cyprus mine is an example; the current price of molybdenum is about 25 percent of what it was when the project was begun. The firm is operating well below planned output level, and houses and classrooms built for expected needs are now excessive.

Changes in the life of a project, whether shorter or longer, have similar effects on local jurisdictions. Changes in project lifespan will affect the local economic, employment and residence patterns. This can result in shortfalls in revenue required for support and repayment of obligations incurred to provide services.

Revenue Sources for Local Governments

Three major sources of revenue are available to local jurisdictions in Idaho for the provision of public services: direct federal aid, property taxes and own source revenue.

Direct federal aid to local jurisdictions is available through several programs including revenue sharing, community block grants and federal payments in lieu of taxes. Direct federal aid has declined yearly since 1978, and some programs are now targeted for elimination. Therefore, it seems unlikely that this source will provide much funding to local jurisdictions in the future.

Property taxes as a source of local government revenue have been curtailed by the "Idaho Tax Revolt" that resulted in the passage of Proposition 1 and its later amendments. Local governments are now constrained to either a 5 percent yearly budget increase or application of current tax rates to 80 percent of the increase in the property market value. In most cases, the revenues derived in this manner are likely to be insufficient for the provision of services required by large scale project construction.

Own source revenue includes both user fees and local option taxes. A user fee is any fee, charge or dedicated tax that is paid by those benefiting from a facility or the service it produces. Examples of user fees include licenses, tuition, water fees, garbage disposal and gasoline taxes. Faced with restraints on property taxes, many local governments have increased their reliance on user fees. In the case of large scale growth, user fees have one important caveat: the uncertainty impacts discussed earlier make user fees a somewhat dangerous funding mechanism. Unforeseen decisions concerning a project are likely to affect public service demands and hence revenues. Drops in projected revenues may lead to a rapid deterioration of the jurisdiction's financial situation.

Local option taxes are levies other than property taxes that may be imposed by and for local governments. In Idaho, their use is currently restricted to resort cities with populations of less than 10,000. Taxes on hotel-motel use and liquor-by-the-drink have gained the necessary 60 percent voter approval in a few such cities. In 1984 the legislature authorized the option of levying a tax on all retail goods, but the restriction to cities of under 10,000 population where tourism is the major industry still applies.

Needs and Alternatives

Idaho's fiscal structure does not contain provisions for the alleviation of the impacts of growth; these must be borne by the existing structure. At the local government level, it seems apparent that the present fiscal structure is barely adequate to deal with the long-term provision of public services for current levels of population and economic activity. When growth occurs the problem becomes much more acute.

Many western states have adopted measures to alleviate the fiscal impacts of growth. Colorado, Wyoming, North Dakota and Montana have developed specialized mechanisms for dealing with large scale projects and fiscal impacts. North Dakota, Montana and Wyoming have initiated comprehensive programs for regulating industrial siting. Under these measures, industries are required to submit detailed planning documents characterizing their proposed projects and estimating the likely impacts of these projects. Oversight groups are empowered to require impact abatement measures such as housing and public infrastructure construction. Permits may be denied for noncompliance.

Colorado, Montana and North Dakota have initiated programs specifically aimed at assisting local governments affected by growth. Colorado has a state severance tax on coal, oil shale and molybdenum; an oil shale trust fund, a local government severance tax and a local government mineral impact tax. Montana and North Dakota have earmarked a substantial portion of their states' severance taxes on minerals for the use of impacted local governments.

Idaho's fiscal and legal structure lacks many of the protective regulatory provisions found in other state codes. Given the potential for large scale projects and the present legal structure, future development seems destined to cause serious fiscal impacts in the state. The experience of other states can be useful in identifying fiscal programs and legal requirements best suited to Idaho. Several alternatives need to be explored and the most appropriate ones adopted in order to mitigate the large scale development impacts that can be expected.

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