

State Notes

TOPICS OF LEGISLATIVE INTEREST

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Local Government Consolidation: Assessing the Evidence for Cost Savings and Economic Improvement **By Eric Scorsone, Senior Economist**

"Encouraging, and if need be requiring, local units of government and school districts to share or consolidate administrative services and deliver them more cost effectively. Michigan has more than 1,800 local units of government and 553 school districts, another 230 charters, and 57 intermediate school districts." Governor's Emergency Financial Advisory Panel 2007 Report

"Facilitate and provide incentives for sharing of services (vertical and horizontal integration) and/or consolidation across local units of government" Legislative Commission on Governmental Efficiency 2009 Report

These statements and many others continue to bring to the fore the issue of government efficiency, cost savings, and the number of units of local government in Michigan. Since the release of the report of the Legislative Commission on Governmental Efficiency and certainly far before that as well, there has been much talk of the policy idea of the merger or consolidation of local governments in the State. This policy idea is most often discussed today in the context of addressing the severe fiscal stress on local governments brought on by falling revenue sharing, loss of population, and declining property tax revenue. This paper explores the possible costs and benefits of such a policy option by reviewing the existing evidence on local government consolidation from other states and countries.

As a reform idea, one of the central goals of intergovernmental cooperation and consolidation is the restructuring of government services in order to reduce costs or slow the growth rate of costs while still maintaining a reasonable level of service capacity and quality. Generally, in the case of a situation of fiscal stress, governments are faced with the uncomfortable choice of cutting services (and costs) or raising taxes and fees. Intergovernmental cooperation and consolidation, among other reforms, attempt to cut this knot by restructuring services and operations to maintain capacity while reducing costs.

In short, one policy question is whether a more fragmented state with a greater number and complexity of local government units will be more expensive and costly compared with a state with fewer units of local government. The issue of cost and efficiency can be subdivided into two questions: 1) the impact of political consolidation or a reduction in the number of units of local government on cost, and 2) the impact of specific service cooperation and consolidation on cost.

However, cost may not be the only issue. Another prominent rationale behind local government consolidation is that the economy will be better in a less fragmented region or state compared with a more fragmented one. This third policy question relies on the assumption that a less fragmented region or state will be more efficient, resulting in a better business climate and improved economic performance. This article attempts to assess the evidence regarding these three policy questions.



Michigan's Local Government System

Before assessing the evidence, it is useful to map the local government system in Michigan. Michigan has what is known as a two-tier system of local governance. One tier is county government which is generally responsible for courts, prosecutor and public defender offices, public health, sheriff and jail operations, drain commission, property equalization, county roads, and a variety of other tasks. In the second tier lie the cities, villages, and townships. Cities and townships are mutually exclusive units while villages overlap with townships. Cities, townships, and villages are generally responsible for water and sewer services, police and fire protection, property tax collection and assessment, urban roads and streets, parks, and other items. Michigan residents live in a county and either reside in a city, township, or village (township) combination. Counties, cities, villages, and townships are known as general purpose governments because they provide a wide range of services.

There is a third hybrid form of local governance which is known as the special district government. Excluding schools, which are special district governments also; these entities are established by general purpose governments to provide a specific service such as a water or sewer authority, fire authority, library district, or recreation authority, among other options. Technically, they are part of the second tier of governmental units but function only for that specific purpose. In Michigan, almost all special districts are governed by a board appointed by one or more general purpose governments. In many cases, special district governments are the key mechanism through which intergovernmental cooperation is achieved for a specific service.

In raw numbers looking across these tiers, Michigan does contain a large number of local government units.¹ Based on those raw numbers, Michigan ranks 14th among all states with 2,314 local government units (see [Table 1.](#)) The number of Michigan special districts has grown over the past few decades, albeit at a slower rate than many other states.

Table 1

Local Units of Government in Michigan	
Type of Government	Number
County Government	83
City/Village Governments	533
Township Governments	1,242
Special District Governments	456
Total	2,314

Source: 2007 Census of Governments

Local Governments and Spending Across the States

The first policy question to address is whether reducing the number of local governments will slow the growth rate of spending in this sector. In terms of spending per person, the best approach is a state-by-state comparison across all types of local units of government. Using this approach, Michigan ranks 14th among all states based on the 2007 Census of

¹ For purposes of the analysis presented here, school districts are excluded due to their special nature and funding sources.



Governments (see Table 2). This ranking translates into \$4,609 per person. Of course, this is an average and would vary widely depending on where a person lived and worked. New York State is the highest spender with an average per capita local government spending rate of \$7,996 and the lowest is Hawaii with a per capita spending rate of \$1,896. The average for all states is \$4,253 per person.

As shown in Table 2, there is no clear relationship between spending per person and total number of local governments or number of persons per local government. New York has the highest spending per person of any state. Of course, this information is skewed potentially by the inclusion of New York City, which is unique in the scope of its services. Meanwhile, Illinois spends only half as much as New York on local government and has more than twice the number of local units of government, including the City of Chicago. The basic problem with these national comparisons is the difference in the scope of service responsibilities and taxing authority given to local governments. A better approach may be to compare similar states, such as those from the Midwest or Great Lakes region, which is what we turn to next.

Table 2
Local Governments and Spending Across States

State	# of Local Units	Persons Per Local Government	Population	Local Spending Per Person
New York	2,918	6,697	19,541,453	\$7,996.30
Wyoming	1,153	472	544,270	\$6,895.89
California	6,574	5,622	36,961,664	\$6,688.23
Nebraska	2,876	625	1,796,619	\$6,003.40
Alaska	1,189	587	698,473	\$5,506.45
Florida	2,197	8,438	18,537,969	\$5,153.53
Washington	2,754	2,420	6,664,195	\$5,119.87
Colorado	3,988	1,260	5,024,748	\$5,034.85
Minnesota	3,185	1,653	5,266,214	\$4,966.83
Nevada	309	8,554	2,643,085	\$4,952.47
Illinois	6,082	2,123	12,910,409	\$4,914.37
New Jersey	1,043	8,349	8,707,739	\$4,830.44
Tennessee	964	6,531	6,296,254	\$4,802.50
Michigan	2,314	4,308	9,969,727	\$4,609.26

Source: 2007 Census of Governments



Table 3 shows that Michigan has the fewest number of local government units in the Great Lakes region². In contrast, Illinois has the highest number with 6,082 local government units. Illinois has a large number due to its extensive use of special district governments. In fact, Illinois is ranked first among all states for the number of local units of government. These raw numbers, however, may be deceptive. More importantly, related to the question posed at the beginning of this article, is there a relationship between number of units of local government and per-person spending?

In fact, as Table 3 reveals, there is no clear relationship between those two variables. Illinois, with many local units of government, spends nearly the same as Michigan, with the fewest local units. The number of local governments does not appear to make a significant difference on spending per person. For example, the state of Illinois has almost 7,000 governments compared with fewer than 3,000 in the State of Michigan. Illinois has such a high number due to the extensive use of special districts compared to Michigan. Again, the evidence does not seem to suggest that there is a strong relationship between number of local units of government and spending per person.

Table 3

Total Local Units of Government for select Midwestern States		
State	# of Local Governments	Local Government Spending Per Person
Illinois	6,082	\$4,914
Michigan	2,314	\$4,609
Ohio	3,034	\$4,521
Wisconsin	2,679	\$4,508
Pennsylvania	4,356	\$4,417
Indiana	2,939	\$4,074
Minnesota	3,185	\$4,976

Source: 2007 Census of Governments

Looking across these Midwestern states, all of which have a similar governmental structure and system, per-person spending is nearly identical considering the wide variation in the number of local government units. This evidence at least throws into question the assumption

² According to a widely used measure of state-local centralization, Michigan ranks as a more decentralized state, which is termed a "local services" state. The general categories range from centralized to decentralized. A state like Hawaii is classified as highly centralized and this matches its ranking as the lowest spending state per person on local government. On the other side, New York is the highest spending state on local government and is also classified as the most decentralized state. Michigan looks more like New York than Hawaii. Other Midwest states are ranked as more balanced such as Illinois, Ohio, Indiana, Minnesota, and Wisconsin. Given that the Midwest states all cluster around being balanced or more decentralized, it would appear that a comparison of local government spending per person is a relatively fair comparison. A different approach to assessing government fragmentation was developed by David Miller of the University of Pittsburgh called the Metropolitan Power Diffusion Index (MPDI). According to this index, the Detroit Metropolitan Area did rank highly, eighth among all metropolitan areas, in terms of fragmentation. However, for the State as whole, Michigan did not even rank in the top 15 for degree of local government fragmentation.



that local government consolidation is likely to result in lower spending or cost savings. Other evidence and more detailed analysis is required to test the assertion that consolidation will result in the outcomes posited.

Intergovernmental Cooperation and Consolidation in Michigan: A Policy Analysis

Having reviewed the overall structure of local government in Michigan and across a variety of other states, a more detailed investigation of individual government services may be constructive. A second policy question is whether, via consolidation or intergovernmental cooperation of specific governmental services, Michigan could reduce the growth rate or actually reduce this per-person spending number. From an economic benefit cost analysis perspective, the second and related question is whether there are policies that are more cost effective in achieving this same outcome. In other words, would alternative policies achieve cost savings in a more efficient or effective manner? The next best alternative would be the internal restructuring of government agencies by a unit of government to reduce costs and improve efficiency. Such activities might include streamlining, adopting lean management strategies, and other changes.

To this point, the evidence seems to point to the fact that a policy of local government consolidation may not be effective in reducing or slowing the growth rate of governmental costs. However, local governments are not monolithic; in fact, they provide a wide variety of services that vary across the types of governmental units. Each of these services presents a different profile and some services may present input opportunities for consolidation and cost reduction. Table 4 provides a brief summary of the types of services delivered by local governments based on spending patterns.

Table 4
Local Government Spending by Category 2007
(Dollars in Millions)

Service Categories	Local Govt. Spending
General Government.....	\$2,187
Social Welfare	4,635
Education and Libraries	529
Transportation	2,761
Public Safety	3,768
Environment and Housing (including sewer)	3,788
Utility and Transit	3,402
Total.....	\$25,601

Source: 2007 Census of Governments

It should be noted that the criteria upon which one judges the potential benefits of government consolidation must be clarified. Efficiency is generally defined as an improvement in the productivity of government operations as producing more outputs or outcomes from the same amount of input. Efficiency refers to doing an existing task better. Effectiveness is defined as whether the right set of governmental services or tasks are being performed.



Further, in thinking about governmental consolidation, it is useful to divide up government operations into categories. Labor-intensive services are those that require more human input as opposed to the use of capital and technology. For example, while technology has enhanced the ability of police personnel to combat crime, it remains necessary under many best practice strategies to employ police officers. In the case of the fire department, a greater use of capital and technology has complemented the protection of property and people. Thus, some services may be characterized as capital intensive. Finally, some services may require a skill or human capital intensive element to them. This for example could include information technology operations, financial operations, property assessment, some police and fire investigation services, and the prosecutor's office. These services require a high degree of training and education.

For labor-intensive services, the evidence suggests that it is difficult to merge and improve efficiency of these operations. In fact, 2009 Nobel Laureate in Economics Elinor Ostrom found in her work that smaller police operations were more efficient than larger police operations (Ostrom, 2009). The reason behind these findings is that an expansion of population is not likely to result in the ability to reduce numbers of employees without directly reducing service quantity or quality by its very nature. These types of services might include police patrol, some general government or city hall functions, code compliance, and similar activities. One caveat to this finding is that any specific local government may be operating inefficiently and a consolidation may result in improvements. However, this change also could be achieved by internal restructuring in some cases.

For capital-intensive services, it is often presumed that a local government consolidation or cooperative effort will result in cost savings. Cost savings may occur due to enhanced purchasing power through bulk purchasing. Of course, in this case, the issue is whether the units of local government purchase the same types of equipment or materials to achieve bulk purchasing power. Another source of cost savings in the case of capital intensive services may be the better use of existing equipment or technology. Two units of local government may both have fire apparatus that are underused and better utilized in a larger jurisdiction. These services include fire suppression, information technology and geographic information system (GIS), water and sewer services, road maintenance, and others.

For skill-intensive services, it may be useful to consolidate across governmental units due to underutilization based on workload in any governmental unit. For example, a court administrator or information technology expert in one jurisdiction may be underutilized based on caseload analysis and it makes sense to combine court personnel. These types of skill-based sharing arrangements are already beginning to occur across local jurisdictions both in terms of personnel and equipment and capital. These services might include high level property assessors, information technology and GIS personnel, librarians, court officials and judges, financial officials, and others.

Thus, in the arena of intergovernmental consolidation of specific services, local and state government policy makers may find it advantageous to address these issues and reduce costs and improve effectiveness. Michigan has certain policies that continue to raise the transaction costs of intergovernmental cooperation activities. At a minimum, it is likely to be



a better strategy for local governments to pursue service specific arrangements before considering political consolidation.

Local Government Consolidation and Economic Development

A third policy question is whether a consolidated form of government, whether a metro-type government or simply the consolidation or a more intensive degree of regional cooperation, may result in a higher level of economic performance. Feiock and Carr (1997) found that the Jacksonville/Duval County merger did not result in improved economic outcomes. Savitch and Vogel (2010) found that, after several years, the Louisville/Jefferson County merger has not resulted in an economic improvement. Based on the available evidence, local government consolidation does not appear to boost a local economy. Contrary to these studies, there is evidence that the economy of Indianapolis performed better following consolidation. The evidence for or against improvement in a local economy is unclear at this time.

A Successful Consolidation: Iron River, Michigan

The case of Iron River, Michigan is an example where local government consolidation has apparently worked, at least five years after the fact. The feasibility analysis indicated that Iron River, post consolidation, should be able to save significant dollars. In fact, research has shown, five years later, that this consolidation did in fact result in lower costs on a per-person basis (Scorsone and Martin, 2010). The economic development outcomes are unclear in this case. Therefore, as stated above, while the burden of evidence may suggest that local government consolidation will perhaps not produce improvements in cost or efficiency, there are certainly cases where it may work.

Despite the success of Iron River, Michigan, the question remains as to the most cost-effective policy needed in order to reduce governmental expenses over time. A policy of intergovernmental government or consolidation should be compared with other alternatives such as internal restructuring or the shifting of services between tiers of government. At this time, very little evidence exists as to the relative effectiveness of these policies. This remains an arena for expanded investigation and research.

Summary and Conclusion

Local governments in Michigan face a severe fiscal crisis following the Great Recession of 2008-2009. Property tax revenue is depressed and likely to continue falling for several years into the future. State revenue sharing has been cut significantly and local option taxes remain highly restricted. Personnel expenditures, particularly those related to health care, continue to rise, creating structural budget deficits. In this fiscal environment, major reforms and restructuring are likely to be ongoing topics of policy discussions. One option is to simply raise taxes; another is to cut spending and reduce services. Beyond those two options, local governments and State policymakers face the challenge of identifying reforms that may be able to reduce costs while still maintaining public services provided. Intergovernmental cooperation and consolidation is one of those reforms.



The evidence presented here suggests that there are significant challenges in using the policy reform of intergovernmental cooperation and consolidation in attaining cost efficiency. In her 2009 Nobel speech, Elinor Ostrom stated, "Complexity is not the same as chaos" in reference to her own work regarding the relationship between local government structure and the efficiency and effectiveness of services. It would be wrong to argue that evidence presented here states that there is never a case for local government consolidation or cooperation. In fact, given the diversity across places and local governments, one should always proceed with a careful analysis of the costs and benefits of local government consolidation or cooperation in that particular case. Some cases will find significant benefits from consolidation; others will find the case for consolidation wanting.

A word of caution is in order in assessing the feasibility of local government consolidation or cooperation. It is relatively straightforward to generally demonstrate that two local government entities -- for example, a contiguous township and city -- can be shown to have duplicative positions and equipment. A proposed merger could eliminate these duplicative activities and positions and lead to lower costs and perhaps lower millage rates. The problem lies in the notion of "feasible". The evidence collected here does at least reveal that the implementation of a local government consolidation or intergovernmental cooperative effort is often very different than the proposed changes. Feasibility studies must be challenged to assess the likeliness that their actual proposals and plans will be carried out and maintained by administrators and elected officials over time.

References

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