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Testimony of Jeffrey Fontaine
Nevada Association of Counties
Before the Financial Crises Inquiry Commission

Wednesday, September 8, 2010

Las Vegas, Nevada

Introduction and Background

Thank you for inviting me to provide testimony regarding the impact that the financial crisis has had on counties and the community services they provide the people of the State of Nevada. For the record my name is Jeffrey Fontaine and I am honored to represent the Nevada Association of Counties (NACO) today. I have been asked to address the following topics:

- My views on the causes of the financial and economic crises;
- The length and depth of the economic downturn in the State of Nevada ; and
- The impact of the crises on county revenues and expenditures and services provided to the community such as police, fire and parks and recreations.

I have been the Executive Director of NACO since January 2007 and during the previous 11 ½ years served as the Director and Deputy Director of the Nevada Department of Transportation.

As background, NACO was formed in 1924 and is the non-profit, non-partisan state association for county government officials and staff and is the state affiliate of the National Association of Counties. All 17 counties in Nevada are members of NACO. Nevada's counties range in population from 1,300 residents in Esmeralda County to nearly 2 million residents in Clark County. Clark and Washoe Counties are generally referred to as the urban counties and the others as the rural counties. Two important distinctions that many Nevada counties share are the size of their land area and percentage of federally managed public lands. Six of the 25 largest counties in the United States are in Nevada, including Nye County which at 18,147 square miles is the third largest. Also, nearly 83 percent of the state is public lands, the largest percentage of any state. In some counties over 95 percent of their land is managed by the federal government, primarily the Bureau of Land Management. Even though Nevada contains vast spaces, it is one of the most urbanized states with 87 percent off the population living in the Las Vegas Metropolitan area in the south and the Reno-Sparks Metropolitan area in the north.

Nevada's main economic engine is tourism in Clark County, but other counties are highly dependent on mining, agriculture, manufacturing and other service industries.

Causes of the Financial and Economic Crisis

One of the main causes of the financial and economic crises in Nevada was the collapse of the U.S. housing bubble and its ripple effect. This has affected Nevada in two ways. First, the rapid decline in housing prices has made Nevada the leader in foreclosures and in percentage of homeowners who are “underwater” in their home mortgages. Second, the loss of home equity and lack of consumer confidence across the nation has resulted in less discretionary spending which is vital to Nevada’s tourism based economy. Additional decreases in discretionary income have been caused by increased unemployment and a loss of value in investment funds. People who are worried about their lower net worth and ability to fund retirement, or their job security or are struggling to pay their bills due to having had their salaries or hours reduced have stopped visiting Las Vegas, or at least are spending less when they do visit. Since Nevada’s economy mainly depends on tourism and gaming the decline in the number of visitors and the amount they spend has a direct impact on the state’s economy. Nevada’s reliance on growth, tourism and gaming has made it especially vulnerable to the economic downturn.

Nevada experienced phenomenal growth for many years leading up to the recession and in fact was the fastest growing state in the nation between 1980 and 2006. The population increased from 800,493 in 1980 to 2,495,529 in 2006, an increase of 211.7 percent. All indications were that growth would continue. It is estimated that during the peak growth era the state added 92,564 people in one year, more than 10 new residents every hour, or 7,700 a month. Growth was concentrated in the Las Vegas Metropolitan Area (Clark County), where the population grew from 463,087 in 1980 to 1.8 million in 2006. A solid economy and relatively low taxes and housing prices were the draw. Unemployment was low and even modest wage earners could realize the American dream of owning a home. Things began to change and housing costs began to increase sharply. Between the third quarter of 2003 and third quarter of 2004 the median value of a home in the Las Vegas Valley jumped more than 50 percent, from \$184,300 to \$283,200.

In northern Nevada, Washoe County which includes the cities of Reno and Sparks as well as surrounding communities in Carson City, Douglas County and Lyon County also experienced significant growth. The natural beauty, proximity to great hiking and skiing, low taxes, and inexpensive homes attracted new residents, many of whom brought large sums of real estate equity from the San Francisco Bay Area. The population of the Reno-Sparks Metropolitan Area (Washoe and Storey

Counties) more than doubled from 195,126 in 1980 to 400,560 in 2006, while in Carson City the population grew by 73 percent, from 32,022 to 55,289.

The population of several of the state's rural counties also grew rapidly, and in aggregate increased from 110,258 to 262,141, a 138 percent increase. In four rural counties (Douglas, Elko, Lyon, and Nye), the population in 2006 was more than double the 1980 population. In Lyon County, the population increased from 13,594 in 1980 to 51,231 in 2006 and in Nye County, the population increased from 9,048 in 1980 to 42,693 in 2006.

The mix of new residents included first time homeowners, as well as investors who purchased multiple properties, including high end homes, with the belief that would continue to increase in value.

County governments did their best to keep up with the influx of residents. Revenues were available to build the basic infrastructure to support the new housing and commercial developments that sprung up, as well as parks, libraries and other community services. Public works projects employed thousands of engineers and construction workers across the state. Clark County even undertook the construction of a 53 mile beltway around the Las Vegas Valley, portions of which are interstate highway, using local taxes and fees approved by the voters.

When the recession hit and unemployment rose, many Nevada homeowners could no longer make their monthly mortgage payments. This started the downward spiral of impacts that we see today.

The Length and Depth of the Economic Downturn in the State of Nevada

Nevada leads the nation in unemployment, foreclosures, homeowners who are underwater with their mortgages and bankruptcies. Only the 20-year-plus mining depression of the latter 19th-century and the Great Depression of the 1930s more adversely affected Nevada. We are now approaching 34 months in this recession and unless Nevada's economy turns itself around sometime next year, Nevada's time in the "Great Recession" will exceed its time in the "Great Depression."

The effects of the "Great Depression" were relatively short in Nevada partly because it had major public works including Hoover Dam and the Hawthorne Naval Ammunition Depot, and an extensive federally subsidized public highway construction program. In addition, the state legalized casino gambling in 1931, and further reduced residency requirements for quickie-divorces. By 1935, Nevada had a budget surplus. However, times were much different back then and

Nevada's population grew from 91,058 in 1930 to 110,247 in 1940. Today Nevada's population is approximately 2.6 million, and for the first time in 90 years more people are leaving Nevada than moving here.

While the crisis has affected all portions of the state, the growth counties have been hit the hardest. These include Clark and Washoe Counties as well as Lyon, Carson City, Storey and Nye. Smaller rural counties such as Mineral, White Pine and Esmeralda have also been impacted, but in a less severe way probably because they did not experience the large growth or run up in housing prices. Also, some of the less impacted rural areas have been struggling for years and those county governments have been extremely conservative in their budgeting and expenditures. None-the-less, the current economic conditions have made the prospects for economic diversification in some of Nevada's rural counties even more challenging. One bright spot is northeastern Nevada where the mining industry, particularly gold mining is flourishing. Unemployment in Elko and Eureka Counties the home to active gold mines is less than 9 percent. However, mining is a cyclical industry and as history has shown it is also subject to downturns.

As an illustration of the relationship between growth and economic distress we can compare two rural counties, Lyon County which was one of the fastest growing counties in the state now has the highest unemployment at 19.2 percent and a high rate of foreclosures. Esmeralda County which experienced very little growth has one of the lowest unemployment rates at 8.5 percent, and sufficient reserves to maintain the provision of services.

The question on everyone's mind is, "have we hit bottom yet?" We would certainly like to think so, but there are some indications that the housing market in Nevada could still see a decline. While there appears to be some positive signs across the country economists predict that Nevada will lag any national recovery. Estimates for recovery range from another year to as much as eight years from now. One thing is clear and that is Nevada must diversify its economy. Tourism revenue is down and due to the fact that 39 states now have legalized casino gambling and 48 have some form of legalized gambling people may be more inclined to stay closer to home.

What will Nevada's future economy be and what will jobs look like? The state has staked its future to the development of renewable energy. While Nevada has abundant wind, sunshine and geothermal resources to position it as one of the top states for the development of alternative energy generating facilities, it will take time to realize this economic transformation. Much of the infrastructure needed to

transmit and export electricity must still be constructed. Significant portions of these generating facilities and associated infrastructure are located on federal lands and will require considerable time for permitting. Once constructed, the operation and maintenance of wind farms, solar panel fields, and geothermal wells do not require many workers. The goal of attracting businesses to Nevada that conduct the research and manufacture the components for renewable energy is an important one that will take time to achieve. In the mean time it appears that economic growth will be incremental.

The impact of the crises on county revenues and expenditures and services provided to the community such as police, fire and parks and recreations.

County governments provide myriad services both discretionary and those that are mandated by the state. State mandated services include; courts, voter registration, public guardians, and assessing property and collecting taxes. Other services include; law enforcement, fire protection, utilities, community planning, building and maintaining roads, business licensing, parks, libraries, and senior services. The level of services provided by Nevada's counties varies, but Clark and Washoe have more mandated responsibilities than do the rural counties. In the rural counties, the state provides the majority of health and human services; however, all counties are responsible for indigent medical care and indigent defense.

To pay for these services counties rely on property tax, the largest source of their general fund revenue, sales taxes, fees for service, permits and licenses. Counties with mineral resources receive revenue from the state net proceeds of minerals tax while those blessed with geothermal resources on public lands within their borders receive revenue derived from the lease of those lands. The county share of these revenues is scheduled to expire in 2011. Due to the fact that 83 percent of the land in Nevada is federally managed public lands, all counties receive revenue from the Payment-In-Lieu-of Taxes (PILT) program which is only authorized through 2012. PILT is an important revenue source for rural counties that have a limited tax base. Because Nevada is a "Dillon's Rule" state and their only power is that which is expressly granted to them by the Legislature, counties have very limited authority to increase tax revenues, or even move them among accounts.

An important provision in Nevada's property tax law put into place in 2005 in response to the rapidly increasing property values caps annual property tax increases at 3 percent for owner occupied homes and 8 percent for all others, regardless of assessed valuation (AV). As it turned out, this has stabilized property tax revenues to local governments despite the collapse of the real estate market.

Basically, the amount of AV that ad valorem taxes could not be billed for due to the cap, the abated amount, can be billed until the abated amount is absorbed by the decrease in AV.

However, the abated AV is about to run out which means that property tax revenues to some local governments will begin decline. For a large part of some counties property values will drop to levels below 2004-05, the base year for property tax limits. In Clark County the total AV in fiscal year (FY) 2009 peaked at \$112B and is projected to drop to \$90B in FY 2010 and \$64B in FY 2011. This will result in a decrease in revenue from a peak of \$383M in FY 2009 to a projected \$344M in FY 2010 and \$273M in FY 2011.

Consolidated taxes (C-Tax) which includes sales taxes, as well as taxes on liquor, cigarettes, and real estate transfers make up the second largest revenue source for counties. Clark County's C-Tax revenues peaked in FY 2006 and 07 at around \$340M and are projected to be \$248M in FY 2010 and 11. One of the biggest declines in sales taxes has been in construction related materials and home furnishings.

Carson City C-Tax revenues peaked in FY 2007 at \$26.8M with actual FY 2010 C-Tax revenues coming in at around \$17.5M, for a decline of \$9.3M or almost 35 percent. One of the major contributors to sales taxes in Carson City is new car sale which are down considerably.

Washoe County also saw a large drop in C-Tax revenues from over \$103M in FY 2006 to just under \$77M in FY 2009

Adding to the problem has been the diversion of county revenue by the state to address its own revenue shortfall. Estimates are that the state will be facing a 50 percent shortfall for the 2010 – 2012 biennium. NACO has estimated approximately \$250M in county revenues have been diverted to the state in the last two years. Most of the revenue was from Clark and Washoe Counties, however all counties have experienced the impacts of diverted revenue as well as an increase in costs as a result of recent Legislative actions to balance the state's budget. Counties are concerned that with such a large deficit looming, the state will divert more local revenues and impose new unfunded service mandates.

Counties have been taking extraordinary measures to balance their budgets and have done so in a very strategic and open manner. Clark and Washoe Counties, among others, have sought public input to prioritize services and target expenditures. Clark County even convened a 15-member citizens' "Committee on Community Priorities" designed to reach out to the community through public

meetings, surveys and focus groups, to gather new ideas to address the budget shortfall.

The first cuts made by counties were to programs and projects that were viewed as having short-term and minimal impacts. For example, many public works projects were put on hold. While the rationale that capital projects can wait until growth resumes and the economy improves is a solid one, it has eliminated much needed work for a battered construction industry that has experienced unprecedented levels of unemployment. Personnel costs were also trimmed by freezing vacant positions, attrition, and by offering voluntary buyouts.

After prioritizing services, Washoe County eventually made the difficult decision to cut funding for parks and recreation, and libraries by nearly 40 percent. The funding reduction for libraries means they are now open 25 percent fewer hours per week, and the larger libraries are open only 5 days per week. Lyon County eliminated its Recreation Program, and many counties were forced to dip into their reserves to balance their budgets.

As Nevada sunk deeper into the recession it became clear that counties would have to make deeper cuts and turned to their largest expense, labor costs. Clark, Washoe and some other counties were forced to implement furloughs, salary reductions, and finally layoffs. Many of these reductions were achieved through negotiations with labor unions. At first, layoffs occurred mostly in departments that issued building permits and handled other community development. As an example, in Carson City, building permit revenues were nearly \$1.4M in FY 2007 and plummeted to less than \$400,000 for a drop of almost \$1M in FY 2010 or 72%. Because of the drop in revenues, their staff in the building department went from 12.7 FTE's to 3. In Lyon County the number of building permits issued went from 2,465 in 2005 to 260 so far in 2010. As a result, staff in the county's building department has been reduced to a minimal level.

Departments thought to be immune from personnel cuts were eventually added, including fire departments and law enforcement. Storey County closed a fire station that had recently been built to serve a growing industrial area and laid off 5 firefighters. This represents 25 percent of all firefighters in the county. In addition, the county laid off 5 of their 25 sheriff's deputies.

Like the private sector, the layoff of county employees can create additional strain on those who remain and adds to the unemployment rate. This hits especially hard where the county is one of the largest employers. The need to reduce personnel

and cut expenses has renewed the debate on the size of and sustainability of local government salaries and benefits.

Counties have also used other methods to reduce their expenditures while continuing to provide services. For example, some counties have recruited volunteers to assist in certain programs. Washoe County worked with a local general improvement district for them to take over the operations of a swimming pool to assure that it could stay open. The need to reduce expenditures has also renewed interest in consolidating and sharing government services, and regionalization. Discussions about shared services are taking place amongst the elected officials in both Washoe County and Clark County. Several of the rural counties in northern Nevada are also taking about regionalizing certain services. In White Pine County, the Commissioners recently approved an advisory ballot question to ask voters if the City of Ely and the County should be consolidated.

The reduction in expenditures is impacting the services provided by counties, and ultimately the constituents that depend on them. The challenge for counties during these difficult times is to provide services to an increasing number of families, seniors and others in need who are relying more on county services as the economy continues to struggle.

From March 1997 to June 2010 Nevada's caseload for the Temporary Assistance to Needy Families (TANF) program, which provides cash assistance to poor families, increased by 90 percent from 16,000 to 30,400 compared to the national average of an 18 percent increase since December 2007. Nevada's Medicaid enrollment increased 60 percent from 165,000 to 263,568 compared to the national average of 17 percent. And enrollment in the Supplemental Nutrition Assistance Program (formerly known as Food Stamps) is up 127 percent from 125,000 to 283,683 far higher than the national average of 50 percent.

Even though these programs are mostly federally funded and administered by the State Department of Health and Human Services, counties play a vital role. They are often the points of access and referral to these assistance programs, and provide a portion of the required match for federal Medicaid dollars. More importantly, as the "safety net" in the continuum of social services, counties are responsible for people who are not served by these or other programs. Due to budget constraints the state has at times reduced services and limited the number of enrollees. Additionally, counties provide services for those who not meet eligibility requirements. For example, Medicaid and TANF programs do not serve childless adults under age 65 unless the person is disabled. As stated by Clark County

Social Service (CCSS), “the people we serve are not served by anyone else, and if we didn’t serve them, no one would.”

According to CCSS, last September they began implementing drastic cuts to their Financial (housing) Assistance program that restricted the length of time assistance could be provided. Adults with no barriers to employment can now receive one month of financial assistance in a 12-month period; individuals with some barriers, such as a short-term disability, can receive up to three months of assistance; and those pending Social Security disability can receive up to six months of assistance. Just prior to the start of the current fiscal year, CCSS completed another 15 percent budget cut due to the shortfall in property tax revenue. Between the two rounds of budget cuts, CCSS reduced their budget by about 25percent and their staffing by the same. The budget cuts mean that less people will be served. In December 2008, 66 percent of sheltered homeless received CCSS assistance (4650 households), and funding for CCSS housing assistance will meet only 50 percent of projected need in 2010.

Also according to CCSS they have seen a significant change in the demographics in the last year, with more employable adults and more individuals under age 25 seeking assistance than ever before. They are currently seeing an influx of individuals who have exhausted their 99 weeks of unemployment benefits and have nowhere else to turn for help. They were inundated with applications during the period that Congress debated the extension of benefits. The result of these cuts is reduced services for county indigent clients, increased homelessness, increased medical costs and a strain on non-profit partners in the community.

Non-profit partners throughout the state are seeing dramatic increases in demand. One of the non-profit organizations that work in partnership with county governments is the Food Bank of Northern Nevada (FBNN). The FBNN distributes food to those in need through a variety of programs. In FY 2006 they distributed a total 4,408,618 pounds of food, and in FY 2009 they delivered 8,410,391 pounds of food. Today they are serving 70 percent more clients than three years ago including more families with children. The percentage of their clients below the poverty line is also climbing with over 45 percent this year compared to about 31 percent just two years ago.

Hospitals are also feeling the effects of the economic crises. Twenty out of 34 hospitals in Nevada incurred operating losses in 2009, with University Medical Center (UMC) losing the most of any hospital in the state. UMC, which is operated by Clark County, is the state’s largest public hospital, and the largest

provider of services for Clark County Social Services. UMC has a long history of deficits resulting from its indigent care responsibilities but they are now reporting that the last three-year decline demonstrates a trend unlike anything previously encountered and is directly related to the current economic conditions. One of the causes is a substantial increase in the amount of uncompensated care partially due to reductions in Medicaid reimbursements and patients defaulting on payments. Also contributing to the deficits are the indirect impacts of reductions in the county's social services and the state's mental health services which are driving patients to the emergency room. Also as a result of the economic conditions, patients are putting off check-ups and waiting to address medical issues until their conditions become acute and are more expensive to treat. UMC has been forced to make the difficult decision to eliminate certain services, and is finding it increasingly difficult to provide quality health care.

In addition to the comments I have presented relative to Nevada, I have consulted with the National Association of Counties (NACo) to offer you a broader and comprehensive perspective on issues of concern to most of America's counties.

Local governments across the country are now facing the combined impact of decreased tax revenues, a reduction in state and federal aid and increased demand for social services. Over the next two years, local tax bases will likely suffer from depressed property values, hard-hit household incomes and declining consumer spending. Further, projected state budget shortfalls for 2010 to 2012 will pose a significant threat to funding for local government programs. In this current climate of fiscal distress, local governments are forced to eliminate both jobs and services.

In May and June of 2010, the National Association of Counties, (NACo), the National League of Cities, (NLC) and the United States Conference of Mayors (USCM) conducted a survey of counties and cities across the country for the purpose of gauging the extent of jobs losses. The surveyed local governments report cutting 8.6 percent of total full-time equivalent (FTE) positions over the previous fiscal year to the next fiscal year (roughly 2009-2011). If applied to total local government employment nationwide, an 8.6 percent cut in the workforce would mean that 481,000 local government workers were, or will be laid off over the next two year period. Projected cuts for the next fiscal year will likely increase

as many of the nation's local governments draft new budgets, deliberate how to balance shortfalls and adopt new budgets.

Local job losses are most heavily felt in public safety, public works, public health, social services, and parks and recreation:

- 39 percent of counties report cuts in public safety personnel. For some communities this means fire and police stations that are closed and the potential for reduced capacity to respond to emergencies.
- 68 percent of counties report making personnel cuts in public works.
- 52 percent of counties report personnel cuts in social services and;
- 48 percent report personnel cut in public health services that are critical to local residents in need.

Given that current economic conditions translates into diminishing revenue streams counties are urging the Commission to fully evaluate the fiscal impact any recommendations will have on local governments. Recommendations that ultimately result in cost shifting to state and local governments will only exacerbate the current fiscal strain and will delay recovery. Accordingly, recommendations must avoid creating underfunded or unfunded mandates for state and local governments.

Counties are also urging that the Commission include in its recommendations the requirement that Congress and the federal departments and agencies meaningfully engage local governments to assist in developing next steps so that deficit reduction can be realized while preserving our intergovernmental system.

When the Commission considers reforms to entitlement programs, counties would urge them to bear in mind the fact that Medicaid provides the essential core funding for the local health care safety net for low-income and other vulnerable populations. Reforms which simply shift costs to state and county tax payers are not reforms at all. With that in mind, counties would urge the Commission to include an analysis of the costs to state and local governments of proposed reforms to Medicaid, alongside projections for the federal treasury.

Conclusion

The Silver State finds itself in the grips of a deep economic crisis with dim prospects for a recovery in the short term. The challenges we face will truly test the abilities and fortitude of our people. History has shown that Nevada will take the necessary and decisive actions to recover from the effects of the current economic conditions. I am confident that Nevada's Counties will do everything within their power to help their constituents through these difficult times, and to lead Nevada to a prosperous future.

Thank you again for the opportunity to appear before you today.