

**Written Testimony for the Senate Local Government Committee Hearing
Senate Bill 1157, Amendments to the Municipalities Financial Recovery Act
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Good morning Chairman Eichelberger, Chariman Teplitz and members of the Committee. Thank you for the opportunity to speak today on important revisions to the state's Municipalities Financial Recovery Act, commonly known as Act 47. My name is Gerald Cross, and I am the Executive Director of the Pennsylvania Economy League Central Division. PEL is a regionally based, nonprofit, nonpartisan public policy organization with over 75 years of experience providing technical assistance to local governments and serving as a catalyst for local government reform. PEL also conducts extensive research and analysis on local government issues. PEL Central serves as Act 47 coordinator or as part of the Act 47 coordinator team for seven communities, including the cities of Scranton and Harrisburg. In addition, PEL has prepared Early Intervention Plans for 12 municipalities since 2008. My comments today will focus on the proposed amendments to Act 47 in SB 1157 and HB 1773.

Providing Alternative Taxing Options

The stated policy of Act 47 is to foster fiscal integrity of municipalities so that they may provide for the health, safety and welfare of their citizens; pay principal and interest on their debt obligations when due; and meet financial obligations to their employees, vendors and suppliers. As such, stabilizing revenue is one of the key components of a municipal recovery plan. Currently, Act 47 permits municipalities to petition the Court Of Common Pleas to temporarily increase rates of taxation for earned income, real property, or both, beyond maximum rates provided by law. The temporary increase provides additional revenue while the municipality enacts the provisions of its plan including cost containment and other measures designed to correct structural imbalance. The proposed amendments in SB 1157 and HB 1773 give municipalities additional revenue options, including a court petition to raise the local services tax to a maximum of \$156 in lieu of an EIT increase on residents and nonresidents. While we agree that it is proper to make an increase of EIT and LST mutually exclusive for nonresidents, we believe that it is a mistake to make an increase in the two taxes mutually exclusive when it comes to residents. First, distressed municipalities often need the additional revenue from both sources to stabilize their finances. Second, citizens of an Act 47 municipality have a responsibility and vested interest to properly fund local services to relieve distress where they live regardless of where they work.

Fiscal difficulties are often the product of economic decline including erosion of the tax base. Pennsylvania's current local government tax structure often has limited success in overcoming this erosion. One of the reasons that many municipalities remain in Act 47 is that they cannot survive without the revenue enhancements offered by the program, even if other problems are

corrected. In order to address this concern, we believe that outside of Act 47 reform the legislature should consider allowing all municipalities to at least double the LST as a permanent revenue source. Such a change would result in significant revenue. For example, the city of York would receive an additional \$1.2 million, equal to a 50 percent increase in the EIT. The smaller city of Lock Haven would net the equivalent of a 40 percent increase in the EIT or \$162,908. A higher LST rate would address the reality that local services, which are the crux of the tax, are becoming increasingly expensive. It also speaks to the reality that Pennsylvania's residents live, work and play across municipal boundaries even though local government taxes, for the most part, are limited by those boundaries. Our research points to the fact that the exodus of residents and their tax revenue from Pennsylvania cities, in particular, have left those cities ill-equipped to pay for necessary services. A general increase in the LST would help to alleviate that imbalance.

Early Intervention Program

As I stated previously, PEL has prepared 12 EIP plans since 2008 and so has extensive experience with this program. In our experience, the EIP's comprehensive look at a municipality's finances provides an excellent early warning tool that allows for short-term solutions that can alleviate long-term problems. The components of EIP, including a historical financial review, fiscal projections and management assessment, are typically able to clearly show the cause of current difficulties and are able to predict coming deficits. An EIP report can serve as a "wake up call" to municipal officials, providing for an opportunity to develop strategies and push for solutions before fiscal problems become so severe that an Act 47 designation is warranted. Our recommendation to strengthen this amendment is to provide consistency of expertise by requiring that the consultant performing the EIP is subject to the same qualifications for Act 47 coordinators as outlined in Section 221(b) of Act 47.

Coordinator

As a coordinator, we would raise no objections to the new duties and oversight of a coordinator as outlined by SB 1157 and HB 1773 in sections of Subchapter B, including, but not limited to, the 45-day timetable to issue initial findings, the requirement to elicit comments from a broad range of stakeholders, the empowerment to investigate and negotiate with tax-exempt property owners, and the formal performance evaluation of the coordinator by the Secretary of the Department of Community and Economic Development or his designee. Most of the tasks outlined in the amendments are already occurring as part of the typical Act 47 routine.

Plan Adoption

We also support Section 247.1 of HB1773, which provides for an annual budget process that grants the coordinator a formal role in ensuring that the proposed budget is consistent with the Act 47 plan. One of the current obstacles to Act 47 is overcoming the lack of political will by municipal officials to enact tough plan requirements. There is little the coordinator can do to force compliance other than the counterproductive withholding of state funding, which has only been used once in the law's history. The annual budget provision would give the Secretary of DCED the option to implement Chapters 6 and 7 if the coordinator believes that the budget is inconsistent with the plan. The amendment makes municipal officials much more accountable and forces them to give more than lip service to difficult plan requirements. Similarly, Section 248 and HB 1773 amendments to Chapter 6 grant the Secretary of DCED an additional tool for reluctant municipalities by providing the ability to request a declaration of financial emergency from the Governor should the municipality fail to adopt or implement a plan.

Five-Year Limitation

Amendments that provide for a five-year limitation on distressed status followed by a three-year exit plan are critical to improving Act 47. The limitation is important because it focuses municipal officials on making the necessary structural and financial changes to bring about fiscal stability within a limited timeframe and provides real consequences if the changes are not made. It breaks the unhealthy, addiction-like dependency on Act 47 that is creating a separate class of municipalities with extraordinary taxing powers. However, it also illuminates what has been termed “Catch 47” — municipalities often remain in Act 47 despite improving circumstances because they need the enhanced taxing powers to survive.

Beyond Act 47

Current limitations inherent in the Commonwealth’s local government structure make it difficult to overcome factors that contribute to municipal distress including growing personnel and legacy costs, tax base erosion and outdated assessments. Municipalities are being hamstrung by provisions such as tax rate and boundary restrictions that limit the ability to both engage in intergovernmental cooperation and create regional service areas. Boundary restrictions in particular are problematic since they constrain the delivery of services to an artificially small service area and tax base. Relaxing those restrictions would make offering and paying for shared services between municipalities much easier. Another contributing factor includes Act 111 arbitration rulings that fail to take into account a community’s ability to pay. As a result of these challenges, more municipalities are turning to non-traditional methods to raise revenue such as borrowing and asset sales, which are often just a one-time, quick fix. Our research shows that tax revenue in the Commonwealth’s third-class cities have sunk from 60 percent to 30 percent of their total revenues in the last 40 years with non-traditional revenues often filling in the gaps. Our research also shows that, in some cities, total tax revenue alone has failed to keep pace with the cost of police and fire expenses.

We applaud the amendments in SB 1157 and HB 1773 that grant coordinators new and better tools to help municipalities navigate fiscal distress and return to financial solvency. But we also call on the Commonwealth to investigate reforms such as tax base sharing for the provision of public services that will assist in preventing more municipalities from requiring the support provided by Act 47. PEL research is clear that the problem is growing, threatening once prosperous townships as well as cities and boroughs.

Pennsylvania is at a critical junction. If we fail to reform the way local governments operate, we will see more and more communities unable to claw their way out but plenty of reasons for residents to move out for other states that take a more modern approach to governance.