Testimony for Joint Hearing on Act 47
By Brian K. Jensen, Ph.D.
Pennsylvania Economy League of Southwestern Pennsylvania
Thursday, December 8, 2011

Good afternoon. Thank you for this opportunity to speak to the four committees regarding Act 47. I am Dr. Brian Jensen. I am the executive director of the Pennsylvania Economy League of Southwestern Pennsylvania and senior vice president for civic policy at the Allegheny Conference on Community Development, our parent organization in Pittsburgh. The Pennsylvania Economy League has a 75-year history of conducting independent, non-partisan research and is committed to sound public policy that enhances the competitiveness of the Commonwealth. In my 24-year career at PEL, I have worked to make Pennsylvania local government more efficient, more effective and more competitive economically.

PEL has had direct, working experience with Act 47 since its passage in 1987. PEL offices across Pennsylvania have either drafted Act 47 Recovery Plans or served as Recovery Plan coordinators in eleven of the Commonwealth's officially designated financially distressed municipalities.

Additionally, in 1998, the Governor's Center for Local Government Services commissioned PEL to review and recommend changes to the Municipalities Financial Recovery Act Program. Our study found that Act 47's provisions for addressing municipal fiscal distress had been inadequate over the previous decade and warranted improvement. We found that a number of shortcomings in Pennsylvania law impeded the recovery of distressed municipalities:

- There are two categories of distress: managerial distress results from inadequate, poor or corrupt management practices; while structural distress results from the crippling erosion of tax base. Act 47 has had success in addressing managerial distress but has had relatively little success in addressing structural distress.
- Municipal officials are sometimes unwilling to implement tough recovery plan recommendations. Act 47 has a limited ability to encourage or force compliance with recovery plans.
- There is no limit to the amount of time a municipality can be in the Act 47 program. The Commonwealth's authority to address a given municipality's distress factors are the same in year 24 of the program as in year one.
- Recovery plans can be and often are thwarted by ineffective labor negotiations on the part of the municipality, unwillingness of labor unions to reach contract agreements and adverse arbitration decisions.
- Municipal distress is often exacerbated by regional distress factors. Act 47 does not effectively address the regional factors of distress.
- The Department of Community and Economic Development could better coordinate its economic development functions with its community development activities to focus resources toward distressed and pre-distressed municipalities.
- Distressed municipalities often are served by distressed or fiscally and academically weak school districts. There is no requirement for school districts and municipalities to work together toward general fiscal recovery.

In answer to these findings, PEL's report advanced ten recommendations on modifying Act 47 statutory language and program policies to improve the likelihood of recovery of distressed municipalities in a timely fashion. While the report offered a variety of recommendations on improving Act 47, in the interest of time here at today's hearing, I will mention just one recommendation that we deemed to be crucial to rectifying the fundamental weakness in the program.

That is, the length of time a municipality operates under the Act 47 program should be limited, and the Commonwealth's authority to intervene in municipal affairs should increase the longer a municipality remains in the program. After a sustained effort through successive recovery plans has proved inadequate for restoring financial health, the Secretary of the Department of Community and Economic Development should be authorized to seek court approval to empower a board of control to manage the municipality's affairs. That board of control should have increased control over labor provisions, including designating the plan coordinator as the neutral arbitrator in Act 111 binding arbitration proceedings. Additionally, if distress persists the board of control should be authorized to prepare a boundary change plan at the recommendation of the Secretary.

At the time of our study, in 1998, six of Pennsylvania's then 17 officially distressed municipalities had been in the program for ten years or more and only three municipalities in total had emerged from the program. The report stated: "In its twelve years of existence, Act 47 has clearly not been a successful vehicle for bringing municipalities out of financial distress."

Besides adding nine more municipalities to the Act 47 roster, little has changed in the intervening 13 years since we released our report. Eleven municipalities have spent ten or more years under Act 47. Of the 26 municipalities that have ever been declared distressed under Act 47, only six have emerged in the 24 years since the Act's passage.

But Act 47 municipalities are just the tip of the financial distress iceberg. Many, many more municipalities are financially stressed but have not yet filed for Act 47 declarations.

At the end of the copy of my written testimony that I have provided, you will see a map showing municipalities in Pennsylvania that PEL has identified as suffering from some category of financial distress, whether it be inclusion in the Act 47 program, participating in Pennsylvania's Early Intervention Program, identification as a municipality in the annual PELSW Municipal Stress Index or one that PELSW has determined to suffer from pension plan distress.

You will note that the map highlights far more than the 26 Act 47 municipalities. Financial distress is rampant throughout Pennsylvania: indeed, there is hardly a county that doesn't have at least one distressed municipality. According to our analysis, forty percent of Pennsylvanians live in a municipality that is undergoing some form of financial distress.

Why are so many of the Commonwealth's cities, boroughs and, yes, townships struggling to maintain financial health? I would submit that problems stem fundamentally from outdated and intrusive state laws. While systemic shifts in the U.S. economy have devastated the tax bases of such former industrial centers as Aliquippa, Johnstown and Reading, it is largely the lack of flexibility that

Pennsylvania law offers to local government to act in the best interest of its constituents that undermines the financial health of many municipalities.

State law hamstrings municipal financial health in two fundamental ways: it artificially and counterproductively increases costs; and it simultaneously segregates municipalities into those that can generate adequate revenues and those that cannot.

Rigid state pension laws escalate municipal costs. For example, Pennsylvania law requires cities to offer defined benefit pension plans to police and fire fighters: they are not authorized to offer hybrid systems that would introduce defined contribution plans into the retirement mix. While Americans now live longer, healthier lives and frequently elect to continue to work into their 60s and 70s, cities are required to offer retirement to police and fire fighters at age 50 with 20 years of service regardless of the health of the city's police and firefighters or the city's public safety and financial needs.

Pennsylvania's municipal pension laws have not kept pace with demographic and economic changes. A graph at the end of this testimony shows the local share of Pennsylvania pension costs will escalate more than three-fold in the next five years barring fundamental changes to pension laws.

Binding arbitration provisions likewise tend to escalate municipal public safety costs. The selection process of the neutral third arbitrator, the requirement that arbitration costs not be shared with labor but fall solely on the municipality, and the failure to require arbitration panels to consider the financial ability of the municipality to pay the arbitration awards, all place municipalities at a disadvantage in the Act 111 process.

I want to be clear – we do NOT advocate the abolition of binding arbitration or the curtailment of collective bargaining rights, but we do think that the playing field has for too long been tilted to the disadvantage of the employer, who in the end, of course, is the taxpayer. Pennsylvania will not be able to restore municipal financial heath and sustainability in the absence of reforms to the significant cost drivers of pensions and binding arbitration.

In terms of addressing Act 111 as it affects Act 47 municipalities specifically, the recent Pennsylvania Supreme Court decision makes it absolutely critical that the General Assembly pass legislation to clarify the long standing practice of Act 47 Recovery Plan provisions having precedence over arbitration awards.

A chart at the end of my testimony compares annual pay increases awarded in a Bethlehem police arbitration, where the cumulative four-year pay increase was 21.5 percent, and those provided in a number of Act 47 Recovery Plans, where the four-year cumulative pay increases ranged from 2 percent to 8.2 percent. The dramatic cost differential clearly shows the beneficial effect that Act 47 has had up until now on holding wage increases to manageable levels.

We urge your careful consideration and full support of SB 1321 and HB 1988 that amend Act 47 and clarify that the law applies to arbitration awards in addition to arbitration settlements. The enactment of one or the other of these bills will ensure clarity in the law and maintain one of the most critical and effective tools for containing costs within Act 47 communities.

On the revenue side of the equation, the Commonwealth has established a taxation policy that pits municipality against municipality, creates winners and losers, and fosters a system in which "have not" municipalities host public

services from which they are forbidden to derive tax revenue and that residents of “have” municipalities enjoy at no cost.

Established “core” municipalities, frequently the county seat or settled borough within a county sub-region, typically host a variety of non-profit or governmental institutions, including hospitals, libraries, parks, churches, post offices, schools, colleges and universities and county, state and federal buildings. As such, these municipalities carry a disproportionate burden of hosting property that is tax exempt. Yet to one degree or another, such tax exempt property generally still requires public services. As a result of significant portions of property being tax exempt yet requiring municipal services, our older, more established cities and boroughs are compelled to establish tax rates at higher levels than those of their less intensively developed neighboring municipalities. If Pennsylvania is to solve municipal financial distress, it must address the issue of tax exempt institutions.

Furthermore, many of these non-profit or governmental institutions serve residents beyond their own boundaries, resulting in a free rider situation where non-residents enjoy the services a city or borough is required to provide as a result of hosting these tax exempt institutions but they do not share in paying for those necessary municipal services. Pennsylvania should consider some form of regional or countywide tax revenue sharing.

Stepping back from the current way Pennsylvania organizes local government and looking at it from a 40,000 foot level, it is apparent to me that were the Commonwealth to start with a clean slate, it would not establish all the mandates and prohibitions that exist and impede municipal financial health. Nor

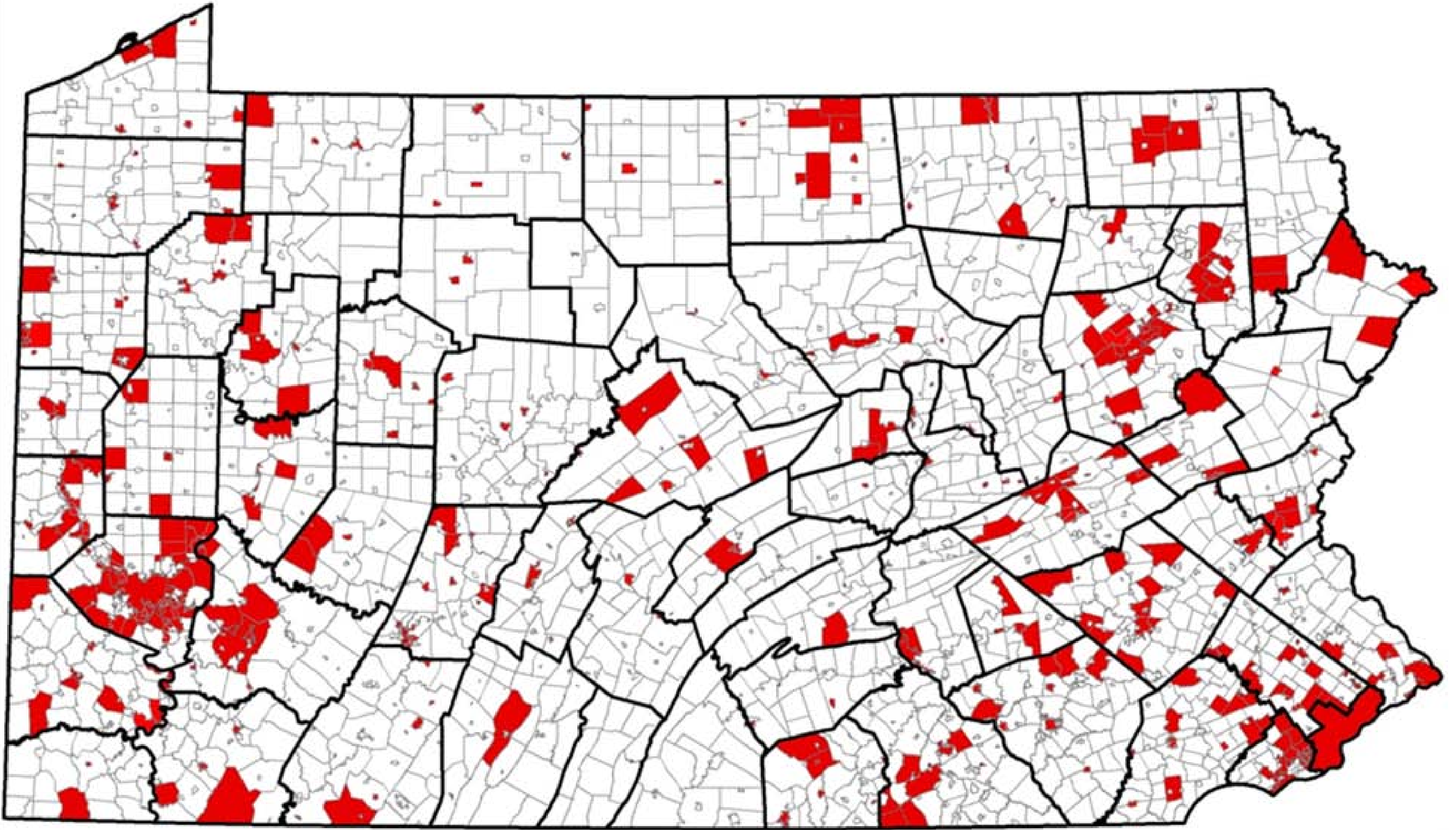
would we establish the boundaries that are currently in place. In some cases, the original reason for incorporation of a city, borough or township and the economic base that sustained it no longer obtain. In short, there are some municipalities are simply obsolete, that the march of progress has left behind.

In these cases, almost no amount of assistance can restore financial viability, and in these cases, the Commonwealth should have a mechanism for liquidating their assets and liabilities and merging them into a neighbor. We would suggest that the General Assembly revisit the recommendation of the State Planning Board to establish a Boundary Review Commission to assist planning the long term disposition of municipalities that are chronically and seemingly permanently financially unviable.

Finally, I would just add that with very limited and shrinking resources the Governor's Center for Local Government Services does a commendable job on a complex set of important issues. If the Commonwealth is to retain the capacity to provide vital services to its municipalities, it must be willing to appropriate funds sufficient to the responsibility.

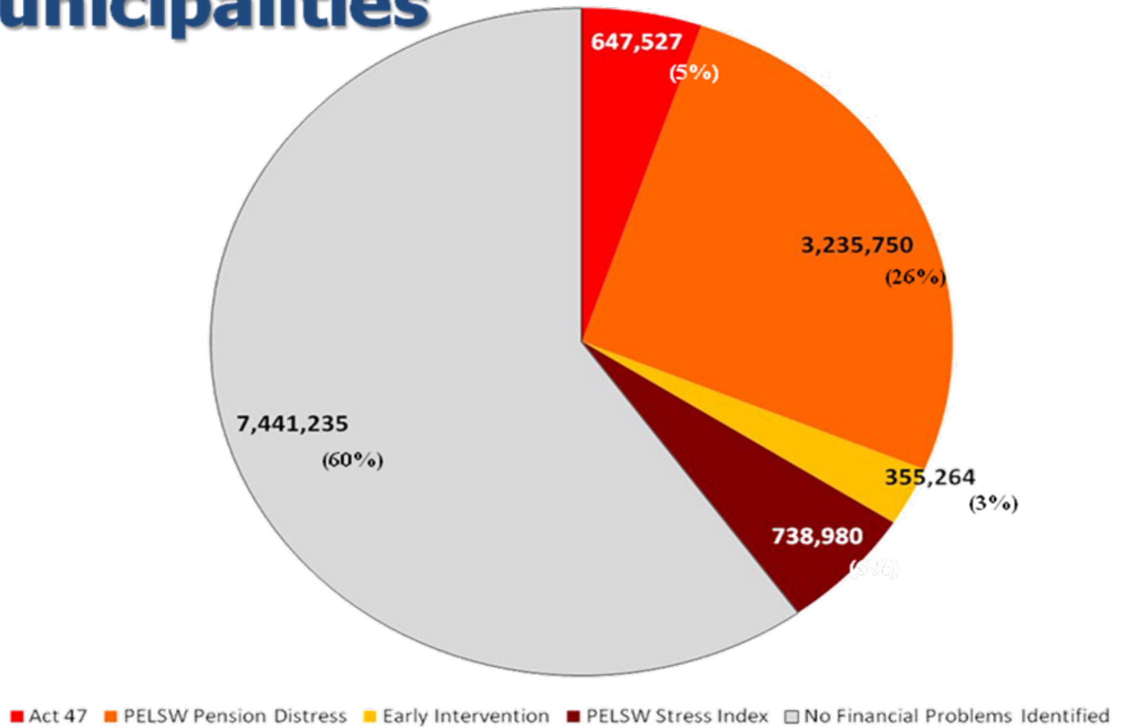
Thank you again for the opportunity to express the Pennsylvania Economy League of Southwestern Pennsylvania's views on the issue of municipal financial distress. I would be happy to address any questions you may have.

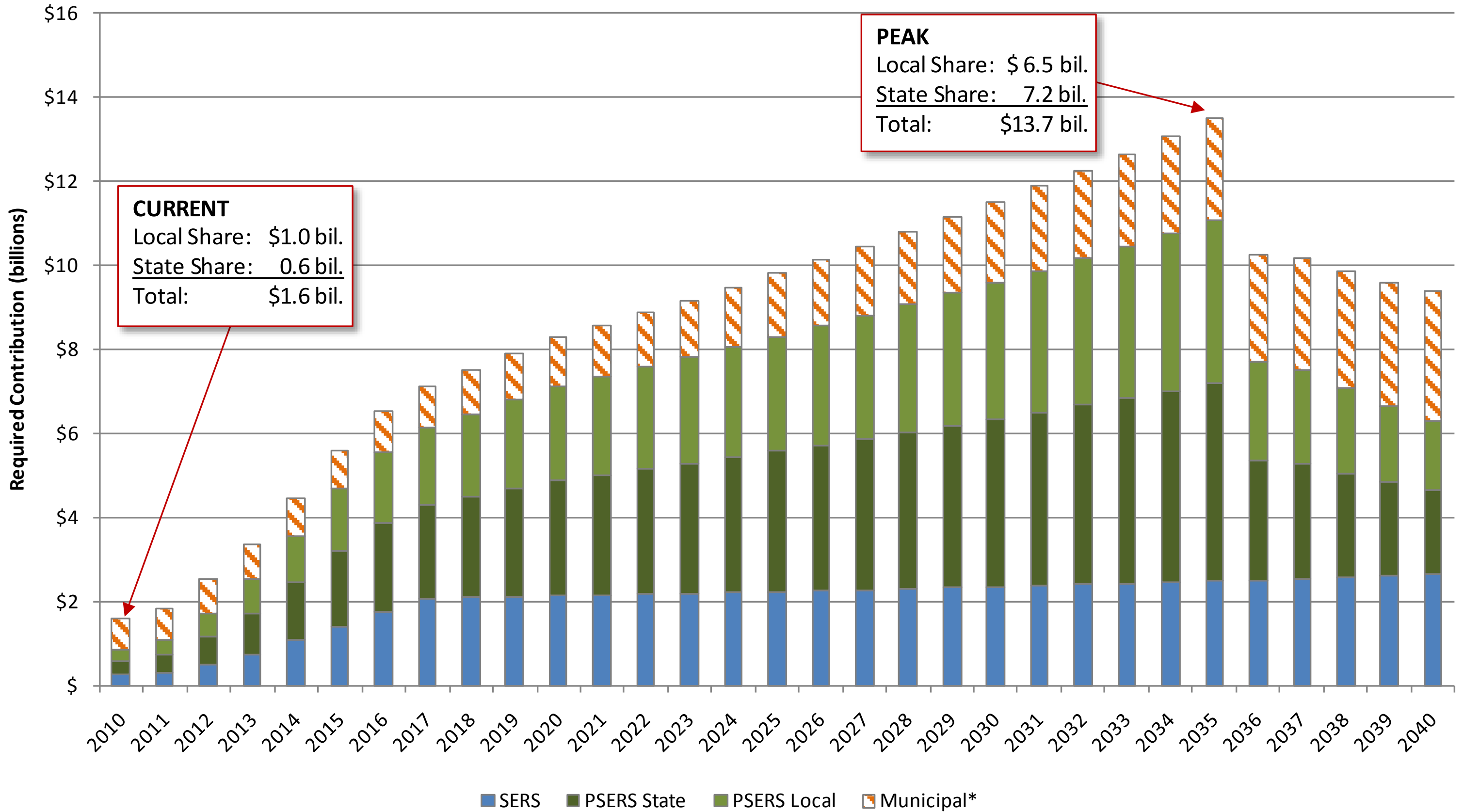
Combined Municipal Stress Indicators
(Pension, Act 47, Act 47 Early Intervention, PEL Stress Index)



Prepared by the Pennsylvania Economy League of Southwestern Pennsylvania, 2011

40% of Pennsylvanians live in financially stressed municipalities




Pennsylvania Public Pensions
(Annual Required Contributions)
PEAK
Local Share: $ 6.5 bil.
State Share: 7.2 bil.
Total: $13.7 bil.
CURRENT
Local Share: $1.0 bil.
State Share: 0.6 bil.
Total: $1.6 bil.
Required Contribution (billions)
$16
$14
$12
$10
$8
$6
$4
$2
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2010
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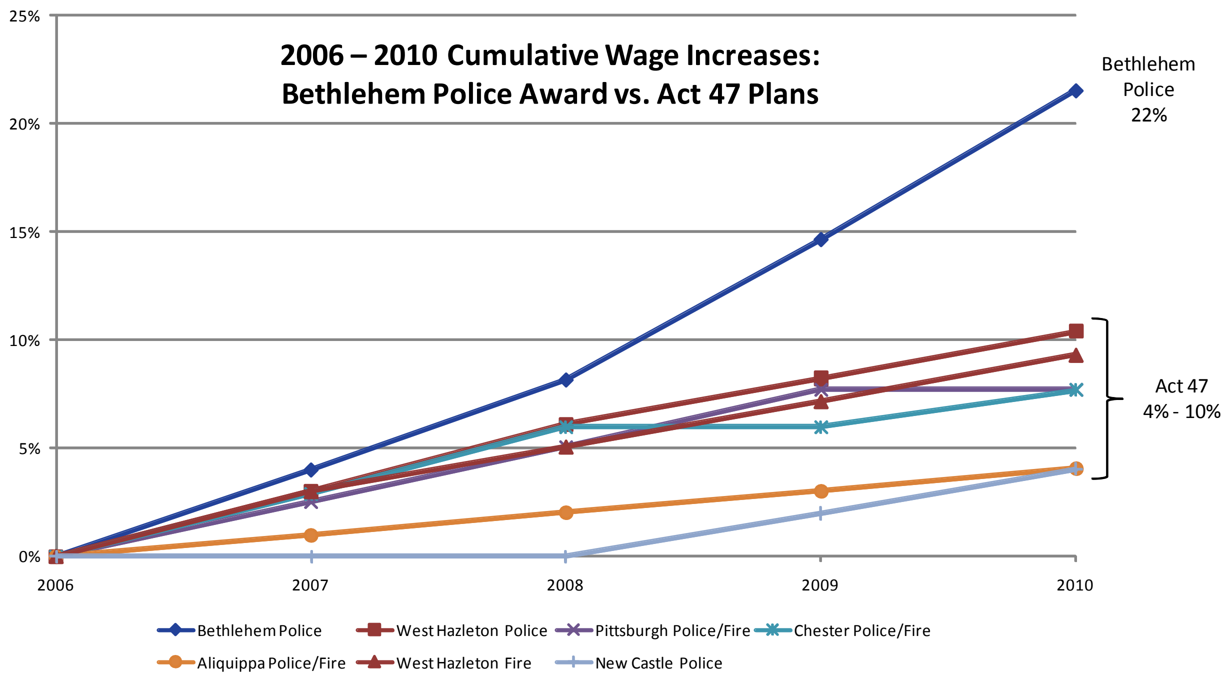
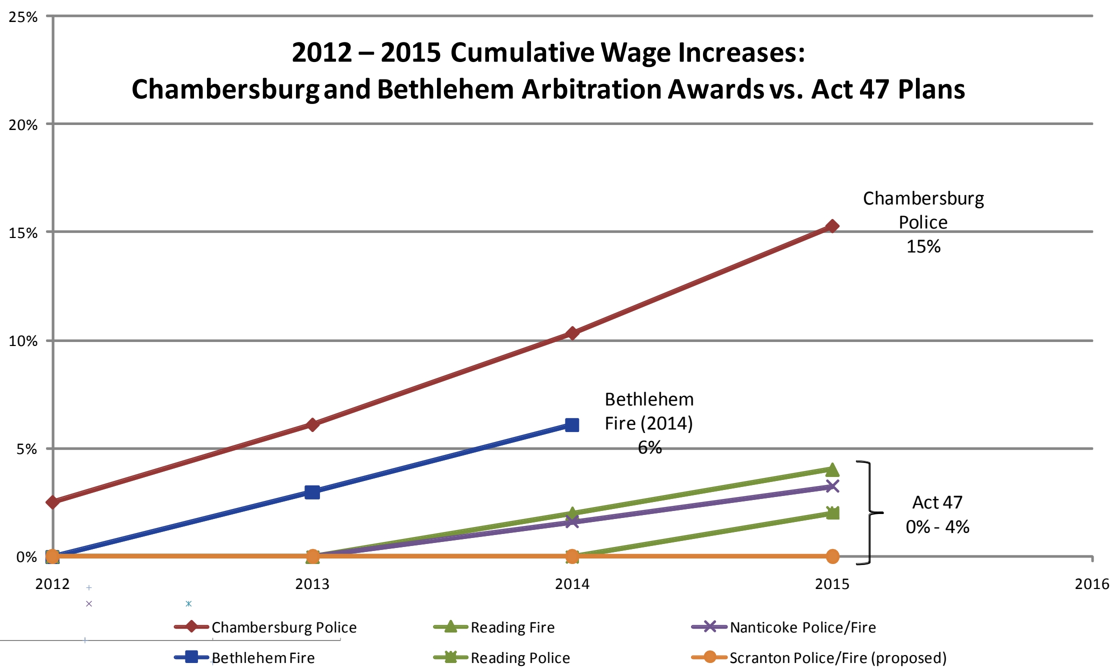
SERS
PSERS State
PSERS Local
Municipal*


2006 – 2010 Cumulative Wage Increases:
Bethlehem Police Award vs. Act 47 Plans
25%
20%
15%
10%
5%
0%
2006
2007
2008
2009
2010
Bethlehem Police 22%
Act 47 4% - 10%
Bethlehem Police
West Hazleton Police
Pittsburgh Police/Fire
Chester Police/Fire
Aliquippa Police/Fire
West Hazleton Fire
New Castle Police


2012 – 2015 Cumulative Wage Increases:
Chambersburg and Bethlehem Arbitration Awards vs. Act 47 Plans
25%
20%
15%
10%
5%
0%
2012
2013
2014
2015
2016
Chambersburg Police 15%
Bethlehem Fire (2014) 6%
Act 47 0% - 4%
Chambersburg Police
Reading Fire
Nanticoke Police/Fire
Bethlehem Fire
Reading Police
Scranton Police/Fire (proposed)