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88 North Franklin Street, Suite 200 • Wilkes-Barre, PA 18701-1393
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Written Testimony for the Senate Finance Committee Hearing
Senate Bill 755, Municipal Public Safety Pension Reform
Gerald E. Cross, Executive Director
Pennsylvania Economy League Central PA Division LLC
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Good morning Chairman Eichelberger, Chairman Blake and members of the Committee. Thank you for the opportunity to speak today. 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 16 municipalities, including recent plans for the City of York and Borough of Shenandoah.

PEL's municipal technical assistance provides historical reviews and projections for General Fund revenues and expenditures. These costs involve typical municipal departments such as police, public works and administration that provide critical local government services to citizens and businesses: public safety, street repair, trash removal, snow plowing, code enforcement and zoning — the list goes on.

But recently we have seen a new department being formed in many communities that threatens to financially swamp all the others combined: the Department of Legacy. The Department of Legacy includes the skyrocketing costs that many municipalities are facing to fund public safety retiree pensions and health insurance. Many remember the financial struggles municipalities had in the past from double digit health insurance increases. Annual cost increases from the Department of Legacy threaten to be worse.

For perspective, in one of our Act 47 cities, health insurance for all employees doubled from $7.0 million in 2002 to $14.0 million in 2010. Pension costs, meanwhile, are expected to soar from $4.1 million in 2010 to $19.7 million in 2020 – an almost five-fold increase. If this scenario remains unchanged, by the year 2020 real estate and earned income taxes would only generate enough revenue to fund the Department of Legacy, debt service and a portion of the police department.

At PEL, we have seen the consequences of ballooning pension payments. For example, Allentown's funded pension ratio dropped from almost 100 percent to approximately 50 percent. The City eventually leased its water system for over $200 million and used the proceeds to shore up the pension system — money that instead could have been used to expand current services, repair infrastructure or pay for other improvements. The City of York has been unable to meet its annual minimum municipal obligation pension payment for years. Increasing pension costs there have contributed to real estate property tax hikes, higher parking fees, employee reductions and more.

Pension distress is not just a big city problem. Of the 25 municipalities with the largest percentage of unfunded pension liabilities, 16 are townships with an average population of 2,600 and five are boroughs with an average population of 1,650. Scranton is the only city in the top 10. And Colwyn Borough, the Commonwealth's newest Act 47 municipality, comes in at number 17 on the list. Of the 1,223 municipalities that administer pension plans, 562 are distressed, according to a recent Auditor General report. These plans are underfunded by almost $8 billion, a $1 billion increase in just two years. These numbers demonstrate that communities of all sizes across the Commonwealth are struggling with a fundamental symptom of municipal distress that will not go away without drastic change at the state level.

Exploding pension costs are coming at the same time that we are seeing a growing problem with municipal financial distress in general. PEL's research and boots-on-the-ground work with municipalities of all sizes shows that Department of Legacy costs are combining with tax base erosion, inflexible taxing options and outdated property assessments, among other factors, to make it increasingly difficult for towns to maintain critical public services and infrastructure. The amount of tax revenue collected by municipalities is simply failing to keep pace with expenditures. This has forced municipalities to balance their budgets through other means that are often detrimental. That could mean selling assets or borrowing money. It could mean not fixing streets or not having a cop on the beat. The bottom line is that the pension problem is exacerbating an already downward financial slide.

At PEL, we believe one answer to the erosion of public services is more movement towards shared services and regionalization. The current legacy cost situation hurts what is already an often difficult and complicated process. For instance, a municipality is less likely to join forces with its neighbor if that neighbor has a distressed pension. Legacy costs also drain money from the system that could be used to create a regional tax base to pay for regional services. Fourteen municipalities are collecting higher earned income taxes from residents and nonresidents under Act 205 to mitigate distressed pension costs. What would happen if that money instead were channeled into a regional public works department that could fix potholes and plow streets over a broader area at a sustainable cost?

Public sector employees deserve to have the benefits for which they worked and were promised. At the same time, the public deserves to have basic services like public works and police and fire protection for which they pay local government taxes. It is critical that solutions are developed now before the situation worsens for both groups of stakeholders.