

April 28, 2009

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Dear Mr. Kaplan and Mr. Roberts:

In the next five years, we have the opportunity to fix our budget crisis. For fourteen years, I have watched as we have ignored, delayed or sought short-term solutions to a long-term, structural problem. As Chief of Staff to a former City Councilman in the 1990's, I watched as Council and the Mayor approved quick fixes, re-financing schemes and tried to find ways to simply push the problem out into the future.

In my second year of elected office, I was the first and only person to call for the City to apply for the Act 47 status to save Pittsburgh from bankruptcy. I couldn't even get a second vote to have the discussion on the issue. One year later, I was joined by former Council Finance Chair Alan Hertzberg to bring the issue to Council's table. Within one month, Mayor Tom Murphy joined with us and a formal request was made to Harrisburg.

For the past five years, I have worked hard to guarantee that the City's finances remained healthy and that we stayed on the course to financial recovery. Last year I was appointed Finance Chairman in order to guide City Council through a new

five-year plan. This new plan must do more than our previous plan. If we are to solve our budget crisis, this new five-year plan must structurally change our City's revenues and expenditures. Anything short of that would only be a band-aid approach to a cancerous crisis.

For the past five years the city has been able to live within its budget because of the Act 47 Recovery Plan. We have been able to reverse our projections from a \$100 million deficit to a reserve fund of nearly \$100 million. However, the same projections that we cite in implementing the first five-year plan; also project a return to growing deficits. The optimistic numbers we have today are the result of difficult choices made in 2004, but we are in the eye of the hurricane. If we fail to use these next five years to make needed structural changes, we will return to the days of growing deficits, service cuts, looming tax increases and malaise for the City and the region.

Our budget is broken – during these next five years, our expenses are expected to once again out pace our revenues, our reserve funds are expected to run dry and our legacy costs will continue to grow larger every year. Without structural changes, we will never be able to get out of this cycle of decline. Taxes to our local population will remain the highest in the region, services will continue to be cut and our tax base of residents and businesses will continue to leave the City's borders. Without significant changes, our problems will grow larger and we will have squandered the opportunity to build a sustainable city.

But, there is a solution. We need to create more than a balanced budget for 2010 – 2014. The budget will need to be a new model of both expenditures and revenues. We need to maintain a constant reserve fund of \$50 million. We need to spend a minimum of \$40 million annually from a pay-as-you-go policy for capital needs. We need to establish a policy of fix-it-first with all of our capital projects. We cannot create any more new debt and we cannot rely on policies of refinancing debt in order to pay the bills. These are the failed policies that created our budget crisis.

There is a way to avoid making the same mistakes twice. It requires sacrifice from all and a willingness to do what is best for Pittsburgh. It requires that we pass a new five-year plan that adopts ALL of the following seven initiatives:

1. Functional Consolidation of Municipal Services
2. Statewide Administered Pension & Healthcare Reform
3. Non-Profit Payroll Tax
4. Regional Revenue Sharing & Local Tax Reform
5. Baseline Audits/ Professional Management/ Outcome Based Performance
6. Control of Long Term General Obligation Debt
7. Initiatives to Create a Competitive Workforce

The most optimistic projection for the next couple of years has our budget just barely balanced. If we pursue this path, we will be doomed to repeat the past. As we continue to pursue a pay-as-you-go policy for capital improvements, our reserve funds are quickly being spent. In order to be able to continue to have a budget that we can live with, without any tax increases or cuts to city services or workforce, and a budget that continues to have a reserve fund to pay for needed capital expenses – we need to find a way to increase revenue by approximately \$40 million and reduce expenditures by the same amount. We need an \$80 million structural change to our budget.

### **Functional Consolidation of Municipal Services**

Pittsburgh needs to be the leader in promoting a new model of regional governance throughout Allegheny County. Any proposal that simply calls for the merging of the City into the County ignores the opinions of national experts in this matter. Furthermore, a City-County only merger would lock legacy costs to present City residents, nearly \$2 billion. That would destroy the City.

Our region leads the nation as the most governmentally fragmented area in the country – we have more government per person than anywhere else and it is costing us tens of millions in duplicative, wasted spending. The City must insist that areas of consolidation should be done only in those departments where countywide consolidation is pursued. In the next five years, we must implement a countywide ERP system and a countywide CIS system - not just for Pittsburgh, but for all 130 municipalities. It is ridiculous to have different information systems for each government. Creating a countywide system and administering it at a countywide level would help to propel other consolidation efforts.

We should pursue with the County the regional consolidation of many, major administrative functions. Payroll, tax collection, personnel, benefits, law and other departments should be moved to a countywide system. During the next five years, plans for consolidation of all administrative functions of municipal governments throughout Allegheny County should be pursued. Some of the easier discussions should be around services the County already offers to other municipalities and unique opportunities for mergers – like RAD parks. With the time we have, we can assure that no one loses their job because of the merger. Some duplicative positions can be eliminated by attrition and others will continue at the county level.

### **Statewide Administered Pension & Healthcare Reform**

The City (and all municipalities) needs to get out of the healthcare and pension business. We need to focus on public safety, public works and neighborhood revitalization. Pension plans and healthcare plans should be administered at the state level and Pittsburgh needs to lead the fight for this reform. By pooling the resources from all municipalities throughout Pennsylvania, older communities that are held back by legacy costs would better be able to invest in their aging infrastructure. All municipalities would be able to leverage greater savings in healthcare costs and better plans for their employees by instituting a single-payer municipal system. Workers would be able to transfer to different jobs and transfer their healthcare and pension plan with them.

We face a crisis today with our pension plan. An independent audit is needed that provides us with an actuarial analysis of our present plan and the impact it will have for our retirees and current workforce. They need to know what will happen if we do nothing. They need to know, from an independent source, the severity of the status quo. A new benefit system will be needed for all new employees during the next five years. Present employees must be given assurances that their pensions will be protected, but they also need independent analysis of what it will take to receive it. We do not have the luxury of instituting new pension bonds in order to make up the deficit. We need an infusion of cash and a new source of increased annual contributions. Mercer has stated that at least \$250 million is needed presently to stabilize our pension crisis – not solve it, just stabilize it. We must look for alternative sources of investments – outside of Wall Street – that provide a return for our pension fund and also a return for our communities. Once we have

stabilized the current crisis, we must immediately work with the state to create a statewide municipal pension fund.

Possibly the greatest savings to the city could come from the implementation of a statewide single payer system for all government workers. Estimates of the savings for the City of Pittsburgh are over \$20 million annually. The ability of all municipalities to combine their resources and utilize one private provider would create a system much like that used by our military forces. The City of Pittsburgh needs to make this and pension reform priorities for a new Pennsylvania municipal agenda.

### **Non-Profit Payroll Tax**

In 2004, the debate over creating a new payroll tax was focused on fairness. The loopholes that were created for the mercantile and business privilege tax made the taxes unfair. It was the goal that we would create a new tax that would affect everyone and would be equal across the board – unfortunately, at the last minute, that bill was amended. Non-profits were taken out of the final version. Pittsburgh and other older cities are the home of regional non-profits - organizations that benefit entire regions and for the most part, are located primarily in one host municipality. Pittsburgh already has a difficult time being able to meet budgets – we have an older population that limits wage revenue, approximately a third of the population lives near poverty levels and entire neighborhoods have diminishing property values. With forty percent of our land owned by non-profit organizations, we are further left with the only option of over-taxing the few who are left to pay the bill for an entire region.

Present Payment-In-Lieu-Of-Taxes agreements have failed. They provide less than one-half of one percent of the annual budget for a city that is host to most of the largest non-profit organizations throughout all of western PA. It is critical that we create a fair payroll tax that applies to everyone. The city of Pittsburgh needs to lead the effort to require everyone to pay the .55% Payroll Tax.

### **Regional Revenue Sharing & Local Tax Reform**

In most cities, revenue sharing is done through income tax. In most cities, you pay a percentage of your income tax where you work and a percentage of your income tax where you live. Most of the cities that do not have this source of revenue have been consolidated into regional local governments. It is almost impossible to find a city that does not have either regional revenue sharing or regional governance. The idea that we all live where we work was forever changed with the advent of the automobile. Unfortunately, Pennsylvania tax code for local municipalities has changed little since then. Even the right to have a commuter tax, which is guaranteed to Act 47 cities, was taken away from Pittsburgh through the Oversight Committee. This outmoded tax policy is why over 20 Pennsylvania cities are under Act 47 and why another 20 could qualify. The combination of fragmented government and the lack of revenue sharing launch us into becoming leaders of disparity between the haves and the have-nots. It is an unsustainable policy that will lead to the further decline of Pennsylvania's older communities – and will continue to allow us to be the national leaders of sprawl and decline.

Unless Pittsburgh stands up for the 53 third class cities throughout Pennsylvania that are facing the same problems as us, there will not be any change. But if we take the lead during these next five years by providing a report of where other cities without regional governance receive their revenue, lobbying the Mayor's of the 53 other cities to join us and then having them lobby their State Representatives and Senators, we just may have a chance to save Pennsylvania's older communities.

On the local front, we need to begin by actively going after those who are not paying their taxes. We need to hire an outside company to research, find and go after anyone who is not paying or who has not entered a payment program for past and present taxes. Local taxpayers are already overburdened with the fourth highest Property Taxes in the County, the second highest Income Tax in the State, the highest Real Estate Transfer Tax in the State and the highest Parking Tax in the country. They shouldn't have to also be expected to pay for their neighbor who has found a way to avoid paying their fair share.

Additionally, we need to implement a Market Based Revenue Opportunities plan that minimizes the impact to our communities but still provides the city with revenue through market based approaches. We should amend Act 77 and merge it with the County – so seniors will only be required to file for their status once and the policy will meet State guidelines. We should amend our Wage Tax to the same policies as the State Income Tax and have both ours and the School District

Income Taxes collected by the State. This will create a uniform policy of income and assist local government in exposing fraud by those who claim more than one address. We should lobby the state to convert the Occupation Tax from a regressive flat \$52 fee to a percentage based model. All of these measures would increase revenue to Pittsburgh, streamline processes and create a more equitable policy.

### **Baseline Audits/ Professional Management/ Outcome Based Performance**

In all of our services and departments there is a very strong need for evaluation and planning, professional management systems and outcome-based performance measures. These policies have been adopted in local, state and federal governments since the 1980s, but have eluded Pittsburgh. You cannot manage what you do not know. We must begin by creating a baseline and a plan for all City facilities. The study should also examine properties owned or operated by all Boards, Authorities and Commissions (including the School Board) and all other government property (County, State and Federal) in order to find the greatest use and savings for the City of Pittsburgh residents. It must take into account guaranteed energy savings programs to save money by investing in energy efficient systems. Likewise, a report is needed on all City vehicles including but not limited to the motor pool, take-home vehicles and cooperative programs like Zipcar. In Parks and Recreation, we need to analyze and plan for our fields and recreation facilities as well as update our aquatics master plan. We also need to establish revenue options for a new Sports Commission that brings amateur and professional events to Pittsburgh and uses the revenue to enhance recreation opportunities for children and young adults.

Other professional recommendations are needed in areas like Risk Management to prevent lawsuits, workers compensation cases, and the creation of a model Fire-EMS cooperation agreement that creates a state of the art first line of defense operation with specific, yet different, operations. Any savings from long-term operations should be used to upgrade facilities and equipment to create the new model. For too many years, City departments have operated without the benefit of a long term plan. In the next five years, we must change that course of action, create baseline reports, implement professional management systems and then hold Directors accountable by annual Outcome Based Performance measurements. Accountability is needed.

### **Control of Long Term General Obligation Debt**

The City's General Obligation debt will continue to represent nearly 20% of our annual budget during the next five years. The only way to reduce our annual debt is to stop creating new debt. But we need to go even further, during the next five years we must avoid the temptation of refinancing existing debt and using the savings for operating or capital expenses. This is not a pay-as-you-go policy – it is a make others in the future pay as we go today. Bonds will be callable during the next five years; we must pay them off and forgo any options that would allow us to use refinancing revenue to pay for current expenses.

Additionally, the City will begin to receive revenue from the new casino this year. Any additional revenue that we receive that is in excess of our projections should be dedicated only to the debt reduction. For the next five years we must do more than simply not create new debt or avoid refinancing debt into the future – we must dedicate additional revenue to debt reduction. If we follow these guidelines, by 2014, we will be in a position to have our debt under control within the following five years.

By 2014, we should also pursue the creation of a State Authority for post-2015 debt refinancing. If the State's bond rating stays at its current level, we will be able to leverage great savings for City taxpayers and restructure our debt sooner, rather than later. If we can be disciplined in the next five years, we will have an opportunity after that to create a livable debt legacy.

### **Initiatives to Create a Competitive Workforce**

In these next five years, we need to create a City workforce that is professionally managed, efficiently organized and competitively compensated. As described earlier, Professional Management Systems must be implemented in each department. Capital dollars must be spent to upgrade equipment, education and training. Analysis should be given to management-worker ratios and each Department should be held to outcome based indicators. The financial plan must reflect truth in budgeting – where employee's salaries and benefits are taken from the Departments and/or Supervisors they report to on a daily basis. Operations must become streamlined to meet organizational charts and all of this information must be public and transparent – both for the workers and the public. All unfilled positions must be eliminated from the budget.

Finally, and maybe most importantly, we need to invest in City workers. We are becoming the training ground for great municipal employees who are leaving the City after we make our initial investment in them. They are leaving for better salaries, better benefits and better administration. We must do more to keep them in the City – this has a direct financial bearing as the constant need for training, especially in Public Safety, comes at a significant cost.

We need to implement a study to determine competitive wages per City job based on regional and national standards. Doing so will require standardizing many positions within the city to lessen the number of pay grades and offer competitive salaries. During this process, no present employee should receive a pay cut – it should be phased in with all new hires. Standardizing pay grades will also help to create uniformity in pay and lessen real or alleged pay discrimination charges. The same study needs to examine the present benefits package we offer to our City workforce and look for ways to enhance it – either through the single-payer statewide municipal plan discussed earlier, or through another collaborative program. We cannot continue to ask our employees to pay more and expect less than Federal, State, County and other Municipal employees. They will leave.

The City needs to expand its preventive health and wellness programs to encourage healthy living habits for the entire workforce. Training and education programs do not exist in some departments. The City needs to continually invest in the knowledge of workers who decide to make Pittsburgh government their career. Those who are dedicated to bettering themselves need to be given every tool to accomplish their personal goals. We will get much more out of them and so will the people of Pittsburgh.

## **Getting It Done**

We have the opportunity to fix Pittsburgh's budget. It won't be easy and it can't be approached like a menu – every one of these steps is needed to create a City budget in 2015 that is strong, sustainable and fair. We have the responsibility to fix Pittsburgh's budget. Every one of these ideas comes with a person, organization or group who will tell us that it can't be done, that it shouldn't be done, or what the negative ramifications will be to the City or those of us who pursue it. We all have an obligation to fix this problem – it needs to be a team effort. It won't be easy and it will come with costs, but by spreading the sacrifice and creating a long-term solution through structural changes, we will fix Pittsburgh's budget problems,

create a model for all of Pennsylvania's older cities and have us back on the road to recovery in just five years. Can we afford not to do that?

Sincerely,

William Peduto

Cc: Mayor Luke Ravenstahl  
Controller Michael Lamb  
President Douglas Shields and Members of City Council  
Henry Sciortino and Members of the Intergovernmental Cooperation Authority  
Acting Secretary George E. Cornelius, Department of Community and  
Economic Development