

14 May 2003

The Honorable Edward G. Rendell
Governor, Commonwealth of Pennsylvania
Governor's Office – Room 225
Main Capitol Building
Harrisburg, PA 17120

RE: Pittsburgh Economic Improvement Task Force

Dear Governor Rendell:

Thank you for asking me to Chair the Task Force responsible for examining the City of Pittsburgh's (City) budget and fiscal situation. This letter report represents a response to this challenge.

The Task Force and I would like to acknowledge the following for their help and support: Mayor Tom Murphy, City Council President Gene Ricciardi, all the members of City Council, City Controller Tom Flaherty and the members and staff of the Pennsylvania Economy League West for their talent and time. We would be remiss if we did not thank Finance Director Ellen M. McLean and Deputy Mayor of Policy and Planning Tom Cox, and their staffs for the information, help, and talent they brought to this task. Attached, for your information, is a list of Task Force members and individuals who graciously assisted us.

History

During the Mayor's terms of office, he has sought to address the City's structural budget deficit. Most recently, in March of 2002, the Mayor appointed a panel of local leaders to study not only the budgets but also to examine the City's finances. The report was of great help in evaluating where the City has been and where the City would like to go.

It is no surprise that revenue structures of cities throughout this Commonwealth do not reflect the reality of the 21st Century. In particular, Pittsburgh's present revenue structure reflects the City as it was in the mid-20th Century, not as it should be in the beginning of the 21st Century. Likewise, expenditures and their rate of growth are rising faster than revenues and their rate of growth.

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Pittsburgh must provide services not just for its own 335,000 residents, but also for hundreds of thousands of commuters who swell the workforce daily. The PGH 21 report summarizes it succinctly:

“The reality 50 years ago was that Pittsburgh had more than 600,000 residents helping to bear the costs for a service-consuming population of more than 600,000. Today Pittsburgh with 270,000 commuting workers, students and visitors daily has 335, 000 residents helping to bear the costs for a service consuming population of more than 600,000. In other words, Pittsburgh is still a city of 600,000, supporting infrastructure and services for 600,000, but without an up-to-date system to recoup its costs.

...

The PGH 21 Committee has concluded that no more one-time solutions exist for this and future budget years and those nine years of cost containment and reductions have not resolved the City’s inherited costs problem. In 2003, the City is facing a potential deficit that exceeds \$50 million (*sic*).”

Findings

The effects of fundamental inequities and inadequacies in Pittsburgh’s tax structure cannot be underestimated:

- 45% of the businesses in the City of Pittsburgh are exempt from business taxes because of historical exemptions granted by the legislature;
- 30% of the property in the City of Pittsburgh is tax exempt, forcing the City to forgo more than \$70 million a year in annual revenues;
- The property tax system which is the largest source of revenue is an unreliable revenue source because assessment valuation is outside the control of city government; and
- 2 out of 3 jobs which accounts for 85% of payroll dollars in the City are held by non-residents, who pay only \$10 a year in occupation taxes, which has remained unchanged since 1964.

The Task Force agrees with the budget gap projections of the City’s Director of Finance:

	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>
Total Revenues	\$357,396	\$362,794	\$368,503	\$381,437	\$391,180	\$397,947
Total Expenditures	<u>\$412,896</u>	<u>\$443,863</u>	<u>\$463,210</u>	<u>\$472,153</u>	<u>\$484,146</u>	<u>\$491,412</u>
Deficit	(\$55,500)	(\$81,069)	(\$94,707)	(\$90,716)	(\$92,966)	(\$93,465)

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The above table reveals the City's critical situation if the *status quo* continues. This table assumes that *no salary increases* are provided after the expiration of the current collective bargaining agreements.

The Task Force acknowledges that the Mayor and City Council have actively worked to address the City's revenue and budget issues, but the City has no other choice but to seek additional areas and opportunities for expenditure reductions beyond those identified in its Fiscal Year 2003 (FY 2003) Operating Budget. The City must intensify its efforts to reach agreements with other levels of government to combine services and resources in order to pare down costs. The City should continue its program of "target budgeting" under which the City would target actual quarterly spending for each department in an amount less than its appropriation, as well as expand the *Citistat* program, which mandates that department heads continually review their expenditures to maximize productivity while pursuing other cost reduction initiatives.

This Task Force is unanimously convinced that structural deficit elimination cannot be achieved by expenditure cuts alone; the tax base of the City is too narrow, with 45% of businesses exempt from business taxes, at least 30% of land tax exempt, and 2 out of 3 employees paying no more than \$10 a year in taxes to support the City's necessary services

Recommendations

The Task Force is mindful the situation in Pittsburgh is different than that found in other Pennsylvania local governments. Pittsburgh's bond rating is solidly investment grade. Pittsburgh's Mayor and City Council have taken the first steps towards alleviating the long-term structural deficit problem by enacting a FY 2003 Operating Budget that calls for significant cuts in expenditures and increases in revenue.

Expenditure reductions totaling \$25.5 million in the City's FY 2003 Operating Budget and \$30.5 million in FY2004, through general government reductions, police reductions, debt restructuring and Fire/EMS merger, must be achieved. We understand that the City is making substantial progress on this front. The general government reductions have been achieved. The debt restructuring program has been completed. Negotiations are underway with Fire and EMS union officials regarding their merger and Police Department savings are on track.

The Task Force believes these first steps, while designed to achieve a balanced budget in the short term (i.e. one to two years), would not be sufficient to eliminate structural deficits in the long term (i.e. five years). The tax structure of the City of Pittsburgh neither effectively addresses the City's needs nor provides the City the means to solve its own financial problems.

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Simply put, the City cannot cut its way to solvency. Although some view cuts to the “bare bone” as preferable to increasing taxes, citizens expect, and rightfully so, that the taxes they are already paying should provide them with the safe, clean streets and quality-of-life services that attracted them to the City in the first place.

While the City’s fiscal situation could be remedied by seeking assistance through the Financially Distressed Municipalities Act of 1987, P.L. 245, No. 47, we believe that the more prudent course of action is through the series of cost reductions and by providing the City with a fair, broad based revenue system.

We do believe that a *Financial Review Board* must be established to assist the City in addressing its fiscal situation. This Board should have sufficient power (*inter alia*) to approve the annual budget and the five-year plan, the right to testify in the collective bargaining process (especially Act 111 arbitrations) and that Act 111 arbitration panels should be obligated to take the City’s ability to pay into consideration. We also recommend a sunset provision for the Financial Review Board, after the City has demonstrated its ongoing ability to maintain fiscal discipline through compliance with the approved annual operating budget and five-year plan.

Although the City has made solid progress to reduce expenditures through workforce reductions as well as holding the line on expenditures, we strongly urge the City to continue efforts at further reductions to include but are not limited to:

- Pursue opportunities for cost savings by merging and consolidating services with other levels of government;
- Expand “CITISTAT” management initiatives to all departments and bureaus to maximize productivity;
- Increase the employee’s share of health insurance premiums to be more consistent with the private sector healthcare through negotiation or executive order, as appropriate;
- Find opportunities for further cost reductions of at least five percent in all departments and bureaus;
- Reduce Public Safety expenditures by completing the merger of the Fire and Emergency Medical Service Bureaus;
- Reduce Public Safety Police costs;
- Reform the Act 111 Arbitration process;

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- Reform the Municipal pension plan and funding.

The *Financial Review Board* must insure that all prudent expenditure reductions be acted upon with dispatch. In addition, state government needs to do its part in this process by authorizing either by legislation or executive directive rules and regulations to bring about necessary changes.

The Task Force recommends that an examination of revenue initiatives should begin. These revenue initiatives, when coupled with further expenditure reduction initiatives, can and will bring about structural balanced budgets both in the short and long term.

Revenue options should be considered not only as revenues *per se* but also as a matter of revenue fairness and equity. The City must be given the tools to implement a revenue system that is both broad based and possess sufficient capacity for growth to resolve the City's structural deficit. In addition to this modernization of the City's tax structure, specific flaws in the current tax structure should be addressed. For example, the Task Force believes that the current Business Privilege Tax (BPT) is flawed in two fundamental ways. First, it is a tax on gross receipts rather than profits which is hostile to the City retaining and growing businesses. Second, enormous loopholes have been created over the years that run against the principals of tax fairness and equity. We favor the elimination of BPT exemptions as a matter of tax equity. **Once equity is achieved, the City should reduce the millage rate of the BPT.** The following revenue options include but again are not limited to:

- Elimination of Business Privilege Tax exemptions;
- Examine the formula pursuant to Act 205 that allocates funds to distressed municipal pension plans;
- Municipal service fee for higher education students;
- Occupational Privilege tax (indexed for inflation annually from 1965 onward with low income and/or part-time exemptions)
- Payroll preparation tax (one half of one per cent);
- Refuse collection fee;
- Retail drink tax (ten per cent);
- Seek legislative authority to establish a Payment in Lieu of Taxes (PILOT) program;
- Use and Occupancy tax;

- Water security fee;

During your tenure as Mayor of Philadelphia, you recognized that success was predicated on the fact that the General Assembly through the Pennsylvania Intergovernmental Cooperation Authority (PICA) legislation gave the Mayor and City Council of Philadelphia access to the experience, knowledge, flexibility and authority critical to Philadelphia's economic recovery. A *Financial Review Board* will be equally of significant value to place Pittsburgh on solid financial footing. Initiatives be they cost saving or revenue enhancing rarely achieve one hundred percent of their targeted goals. Working with the General Assembly, the Mayor of Pittsburgh, the City Council, the County Council, and the civic/business communities, you can help bring about the legislative and political will necessary to achieve the goal by making Pittsburgh.

“... the best place in the world to live, work and do business...”

RESPECTFULLY SUBMITTED,

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BY:

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