PA Municipal League
Testimony Before the House Democratic Policy Committee
Regarding Municipal Tax Burden
February 18, 2020

Chairman Sturla, Representative Flynn, and members of the Committee, thank you for the invitation to provide testimony today. I am Amy Sturges, Director of Governmental Affairs, for the PA Municipal League. I am joined by the League’s Executive Director, Rick Schuettler.

The PA Municipal League (the League) is a non-partisan association representing 116 municipalities from across the Commonwealth. Our membership is diverse. It consists of core communities – cities, boroughs and townships – of varying sizes. The common element among our members is the fact that they are full-service, core communities. As such, they provide a wide range of programs and services to their residents, businesses, tax-exempt entities, workers and visitors, as well as their regions.

The fiscal health of local governments in Pennsylvania is an on-going concern for the League and its members. Over the years we have provided testimony time and time again stressing the importance of addressing the root causes of municipal fiscal distress while also providing new tools to correct and prevent future distress. In 2009, in testimony before this Committee, we quoted a critical statement in the Pennsylvania Economy League’s 2007 comprehensive analysis of municipal revenue shortfall, Structuring Healthy Communities. That statement was, “…fiscal distress is often inevitable under the existing state laws that govern municipalities. Current legislation and codes leave those who lead the Commonwealth’s cities, boroughs and townships with revenue streams that are largely inelastic, capped, and out of sync with budget needs.” This statement is equally true today. Regrettably, over a decade later, nothing has changed statutorily to improve the plight of the Commonwealth’s core communities. As a result, local budgets are
harder to balance, the tax burden is highest on those least able to afford it, and fiscal decline has worsened.

There are a number of factors working in tandem that make fiscal distress is inevitable. As municipalities “mature” in terms of providing a full range of services and becoming built-out, tax revenue begins to slow. Over-reliance on two primary local taxes causes the base to weaken. These municipalities find that they cannot generate adequate revenue to shore up the tax base, therefore finding it difficult to pay for all of the services they provide. Non-essential services are cut first, but as service and personnel costs continue, taxes need to increase and/or the next level of cuts undertaken. Taxpayers – residents and businesses – witness the decline in services while paying more in taxes. This initiates movement out of the municipality to escape the higher taxes and the visible signs of service cuts – blight, deterioration of parks, and inadequately maintained roads, for example. An un-kept and highly taxed community is not attractive to desperately needed new residents and businesses. This results in a cycle of falling property values and income levels that perpetuates more decline and more fiscal distress.

This scenario is further impacted by costs that local leaders have very little control over – tax-exempt properties, unfunded mandates, and personnel. Local leaders seeking to create attractive, clean and safe communities find themselves with no viable solutions to a systemically broken system governed by state laws that are outdated and inflexible. They also realize that only the General Assembly holds the key to new laws and new tools necessary to govern effectively in the 21st Century.

Like the Commonwealth, municipalities rely on tax revenue to pay for the services provided to residents and businesses. The laws governing our local tax structure were written in the 1960’s and have remained largely unchanged. Furthermore, all local taxes are authorized by state statute, capped at certain rates, and are not flexible. Over the past 50 years, municipal services, on the other hand, and the costs to provide those services have changed significantly. This leaves us with one clear fact, outdated revenue sources are not meeting today’s needs.
The majority of local tax revenue comes from two main sources, the Real Property Tax and the Earned Income Tax. As their names imply, these taxes rely on healthy property values and healthy income levels to produce adequate revenue to meet costs. If one examines the budgets of full-service communities, tax revenue is barely meeting public safety costs, which can top 50% or more of a municipal budget. When tax revenue is insufficient to meet costs, the choices are limited – taxes must be raised or services cut. These choices may seem simple on paper, but are very difficult in reality as local leaders look for a balance so as to not dig the fiscal hole deeper.

The decision to raise taxes does not come without a price. The capacity of taxpayers to absorb higher taxes must be weighed against the benefits. If the capacity to pay more is not there, a decision to raise taxes will result in the residents and businesses leaving for municipalities or even other states with lower taxes. The alternative, cutting services, has its own drawbacks and can only be utilized to a point. Once services, such as public safety, are in place and at a certain level, reductions to these fixed costs are very difficult to achieve. It’s easier to delay road and infrastructure maintenance, reduce blight and code enforcement efforts, and scale back on quality of life programs and services. In the end, however, this only adds to the cycle of decline.

The League has long advocated for a more equitable tax local structure that allows local officials to decide the best mix of taxes for their municipality. Municipal officials should be able to pick among a number of different taxing options based on the particular needs and capacity of their municipality and its residents. This would include adding new taxing options, such as a Payroll Tax; but also allowing flexibility within the current system, such as the ability to raise the Local Services Tax beyond $52 dollars or the ability to increase the Earned Income Tax. These need to be local choices based on local needs.

Additionally, expanding the local tax base to a regional level would share costs across a wider area while increasing revenue potential. A regional approach, such as a countywide sales tax, better matches the way we live today traveling in and out of several municipalities each day for work, meals, entertainment, and shopping. Revenue would be shared among the municipalities and the county and could be used for a variety of purposes such as offsetting county and municipal property taxes; alleviating the tax-exempt burden; and supporting regional services.
Compounding the impediments of an outdated and limited taxing structure, the Commonwealth's older core communities suffered a loss of population and tax base 50 years ago. In the 1970's, the attractive suburbs offered new single family homes, lower taxes, better schools, lower crime and job opportunities. Our new and improved transportation systems supported moving further from jobs and services. This out-migration set in motion a loss of tax base and, in turn, a loss of revenue to support established services. The Commonwealth's cities and urban boroughs still struggle to compete with the suburbs, the beneficiaries of the population and wealth shift. Today, many first-ring suburbs are facing the same crisis of cities and boroughs as their population and tax base move to the more far-reaching suburbs.

As population declines, the remaining residents and businesses shoulder an even greater burden of taxation to keep up with the cost of services. Oftentimes, this burden is falling on populations least able to afford the higher taxes – senior citizens and low-income workers. As the cycle continues, tax-burdened residents can no longer afford to maintain their homes leading to blight and abandonment and a further erosion of the already fragile tax base.

In order to reverse the loss of population, municipal officials must work to make their communities marketable and attractive to potential new homeowners and businesses. The housing stock and taxes must be competitive with neighboring municipalities, job opportunities must be available, infrastructure must support the population and crime must be under control. Recreation and cultural activities, good schools and reliable public safety services are also very important to potential new residents. What it takes to turn the tide – community investment and redevelopment; renewed attention to services; and enhanced quality of life factors all cost money, time and resources. A municipality with no tax base is going to be hard pressed to achieve these necessary but difficult goals.

The Commonwealth must become a partner investing in its core communities. The League is an advocate for a direct and comprehensive fiscal urban policy aimed not only at supporting those struggling to regain their footing and re-invent themselves, but also at preventing future fiscal distress. An urban policy would incorporate all of the items being laid out in our testimony today.
Regardless of new taxing options to meet local needs, the expense side of the equation cannot be ignored. Police, fire, emergency services, road maintenance, street lighting, blight remediation, water, sewer and garbage collection are in demand by citizens and are clearly necessary services, but the costs are overwhelming local budgets. As mentioned earlier, in many full-service municipalities, the cost of public safety services alone makes up half of the general fund budget and is barely covered by the tax revenue coming in. It’s important to remember that personnel costs, such as contracted salary adjustments and pension obligations are fixed costs. Therefore, even if a municipality wants to reduce these costs, legally it cannot.

Aside from the operational costs, complying with unfunded state and federal mandates is a significant source of angst for local officials. Oftentimes these mandates are outdated, unclear, and expensive. A few examples of such mandates include: the laws governing municipal advertising; the requirement to pay prevailing wage on public projects costing $25,000 or more; and the requirement to reduce point-source storm water pollution. State government must alleviate municipalities of such outdated, ineffective mandates. Public notice can be achieved equally well by allowing local governments to place their notices on their websites rather than paying thousands of dollars each year to place public notices in physical newspapers that have lost readership in favor of electronic media sources. Prevailing wage should be a local option or at a threshold much higher than $25,000. Taxpayers have spent billions on storm water compliance measures that are changing, unclear and ineffective in the overall picture.

In addition to advocating for commonsense cost control measures, the League supports efforts to encourage service sharing among municipalities and regions. There are many examples of regional service provision across all levels of local government. We believe the Commonwealth should foster these types of service arrangements and assist as necessary to remove impediments. The more successes we have with shared services the more municipalities will consider working together.
Not only does tax revenue pay for municipal services, it also pays for the personnel to perform the services. Pennsylvania’s full-service municipalities are up against staggering pension, healthcare and personnel costs and must attempt to balance these fixed costs with the capacity of the tax base to afford them. Public safety personnel mandates are significant cost drivers that must be included in any discussion of municipal tax burden.

In the area of public safety personnel, the balance tips in favor of the employee and against the taxpayer. Act 111 of 1968, an unfunded mandate, governs the collective bargaining process for police and fire fighters. If a municipality and labor union go to arbitration to have certain items of a labor contract settled, the arbitrators decide an award that is binding on both parties. In this case, the arbitrator has more decision making power and more of an impact on the municipality, than the local elected officials. Unfortunately, there is no consideration of whether a municipality, or its taxpayers, can afford an Act 111 award. Furthermore, benefits can be awarded that were never on the bargaining table. Act 111 must be reformed to level the playing field and give municipalities a fighting chance at controlling their future personnel obligations. Yet, for over a decade, we have not been able to make progress on achieving bi-partisan support for Act 111 reform.

Public safety pensions are another unfunded mandate that tie into Act 111. Municipal pension laws dictate the type of pensions and the benefits to be received. Current public safety pension costs are not predictable or sustainable. This is demonstrated by the number of under-funded plans. In addition to Act 111 reform, the League has been a long-time advocate for municipal pension reform. Among other reforms, new hires should be entering a defined contribution plan and retiring no earlier than age 55. Representative Greiner has again this session introduced a municipal pension reform bill – House Bill 2081. This bill is scaled back significantly from prior sessions and its positive impact would be years in the making, but it is a start and it deserves bi-partisan support.

A final mandate that must be mentioned in any discussion of tax burden is the designation of tax-exempt which is made at the state level, but the impact is a local one. Core communities that host a high percentage of tax-exempt entities face an additional hurdle in maintaining the tax base and staving off fiscal distress. Government buildings, hospitals, universities and cultural centers
provide services to the region, but they do not pay property taxes to their host for the services provided. On a volunteer basis some tax-exempt entities make in-kind contributions or payments in lieu of taxes to their host municipality, but these cannot be relied upon and do not come close to the amount of tax revenue lost. This means their share of taxes is paid by the property owners who already shoulder a large burden as demonstrated throughout this testimony.

We recognize that these institutions contribute to the community; they are often the largest employers. They also serve the region with healthcare, education, cultural and entertainment programming. Possible solutions to the help alleviate the impact of tax-exempt entities are: spreading the cost of services over the entity’s service area; establishing a required payment in lieu of taxes system that includes government owned facilities; authorizing municipal services fees; establishing a fund for state reimbursement to municipalities as put forth in Representative Freeman’s House Bill 1677.

To some, this testimony may be an oversimplification of the fiscal issues impacting the tax burden on residents and businesses in our core communities. Each municipality and its individual circumstances are different, but they are all operating under the same broken system. Purposely, we have left the data and real life examples to the experts – the PA Economy League and the elected officials testifying today. Unfortunately, Mayor Sorace of Lancaster was unable to attend this hearing. She has been sounding the alarm on behalf of for her own city’s fiscal health and we highly recommend the Committee invite her to testify at a future date.

Briefly, Lancaster, a city often held up as thriving, is facing a $20 million budget deficit in just 5 short years. Property Taxes bring in 50% of the city’s revenue while public safety expenses makeup 65% of the budget. Lancaster has increased Property Taxes 8 times in the last 14 years. It has also increased fees, reduced spending, and relied on reserves to balance recent budgets. Its reserves will soon be depleted and extreme tax increases are on the horizon if reform measures at the state level are not implemented. Those in local government see Lancaster’s fiscal situation as a perfect example of the result of a systemically broken system.
In conclusion, elected and appointed municipal officials work tirelessly to make our core communities attractive places to live and work. They put their best foot forward no matter the severity of the circumstances. They work to keep employment opportunities available; to make housing choices attractive and affordable; to provide services and amenities that are competitive with neighboring communities; to keep crime at bay and to provide the necessary infrastructure to support citizens, businesses and visitors. This is a tall order given the fact that they are working with an outdated local tax system, laws that work against good government, and ever-rising service and personnel costs.

The fiscal crisis facing Pennsylvania’s local governments presents all of us, as policymakers, with the unique opportunity to make real, significant change before it is too late. The League and its member communities are prepared to continue this discussion and ready to help find the answers and support the hard choices necessary to see our local governments gain and sustain fiscal health. After all, the prosperity of the Commonwealth is directly reflected in the prosperity of its local governments.