

**STRUCTURING HEALTHY COMMUNITIES
MUNICIPAL CASE STUDIES**

Prepared by:

**Pennsylvania Economy League, Central PA Division
88 North Franklin Street, Suite 200
Wilkes-Barre, PA 18701-1393**

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CHAPTER 1

INTRODUCTION

The Commonwealth of Pennsylvania has 67 counties made up of 2,564 municipalities consisting of 960 boroughs, 1,547 townships, one town and 56 cities. The state constitution categorizes cities by class as follows: Philadelphia is the only first class city, Pittsburgh is the only second class city, Scranton is the only second class A city and there are 53 third class cities. The Third Class City Code promulgates how a city may be organized or a city may use a form of government under an Optional Plan or Home Rule. In addition to the Third Class City Code there are a number of other state laws that affect the cost and provision of city services, for example:

- Act 511 of 1965 – The Local Tax Enabling Act
- Act 111 of 1968 – Policemen and Firemen Collective Bargaining Act
- Act 195 of 1970 – Public Employee Relations Act
- Act 205 of 1984 – Municipal Pension Plan Funding Standard and Recovery Act
- Act 7 of 2007 – Local Services Tax.

While the primary purpose of municipal government, regardless of size or organizational structure, is to provide infrastructure and public safety, the type and level of services provided vary from one municipality to another. Nearly all municipalities primarily rely on property tax, a percentage of the realty transfer tax, miscellaneous fines and fees and many levy an earned income tax (usually shared with the local school district) to provide municipal services. With a strong reliance on the property tax for the majority of municipal revenues, it is important to look at a municipality's home county assessment practices, when that county last reassessed its properties, the common level ratio, and the type of services the county provides for the municipality, for example: libraries, 911, tax collection or recreation.

It is safe to say that all municipalities have some property reported as not subject to the property tax and nonprofit organizations within their boundaries. Parks and recreation areas contribute to a municipality's quality of life. Hospitals, state and federal office buildings, colleges and universities, and local school systems contribute to the economic vitality of a municipality. Local non-government social service agencies and churches meet the emotional,

physical and spiritual needs of the county and municipal population. Often these organizations are established as not-for-profit and the land and buildings they own are not reported for purposes of the property tax. Usually the only revenue a municipality receives from these entities is from the organizations' employees through the Local Service Tax and Earned Income Tax levied upon residents of the host municipality. While some nonprofits have agreements of funding or make payments in lieu of taxes (PILOTs), the payments may be less in comparison to the lost tax value of the properties involved. Also, most PILOTs are voluntary contributions and cannot be relied upon in revenue forecasts for future years, nonetheless, clients and employees of the nonprofits have an expectation of 365 days a year 24/7 services of public safety and infrastructure—for example, plowed streets in the winter, even on weekends.

How do we define a healthy community? Is it based on the appearance of new buildings, preserved architecture, clean well lighted streetscapes, or the availability of safe affordable drinking water or even a conference center? Is it calculated on the employment base, residential neighborhoods and the median incomes of the residents? Is it based on the amount of crime within the municipality and the perception that crime creates regarding one's safety? Actually, it is all of these and one more—the most important one—the fiscal stability of the municipality. If a municipality is not fiscally stable, it cannot clean the streets, keep the streetlights lit, fight fires and apprehend the criminal, much less put water in the municipal swimming pool, mow the grass in the parks or plow the streets.

Based on controlling costs and generating revenue, fiscal stability for a municipality means that on an annual basis, it can pay for the services it provides, meet the required financial commitments for its retired employees, and provide for future capital projects that are part of its infrastructure and public safety mission. How are the third class cities of Pennsylvania doing in this regard? The answer is “not well.” Why aren't these municipalities fiscally stable? The case studies point to a “systemic problem,” not a political or personality based problem.

Reflecting municipal leadership from both political parties, the case studies of Reading, Bethlehem, Lancaster, Easton, and York represent the public policy decisions of mayors, city councils, business administrators and finance directors who balance the municipalities' provision of public services with the requirement to pay for services within the constraints of the applicable laws and available funds. Municipal leaders may be willing to share services across jurisdictional lines but neighboring jurisdictions are either not interested, or more realistically,

don't want to share the costs. The public and municipal leaders greatly value the commitment of their career public employees but the municipal coffers can no longer afford the increasing related health care and pension costs, as well as the normal expected increases in wages.

The case studies demonstrate that state laws, mandatory arbitration awards and court decisions have far reaching affects on the economic health of Pennsylvania municipalities; therefore proving that these municipal fiscal problems are “systemic” and not “political.”

The case studies illustrate the true concerns of elected officials and the career public administrators who can no longer raise sufficient taxes—particularly property taxes—to cover costs to balance the annual budget. When revenues are insufficient, mayors look for one-time strategies such as selling an asset, borrowing money or other creative financial bridges to buy time. (The term “operational supplement” is used in these studies to describe these strategies for the purposes of this report.)

There is a limit to how creative mayors may be under state law, the credit market willingness to lend and the depth and experience of their financial staffs. Municipal officials of the studied cities are good leaders and public administrators. The common perception is that these cities are fiscally sound, but in fact, the case study municipalities are on the edge of financial distress. Municipal leaders are running out of one time operational supplements to balance the annual budget. Other municipalities are even faced with invoking Act 47 and reducing or eliminating services. Even while “right-sizing” may be an opportunity for an annual budget, municipalities must forecast future revenues and expenditures within the legal parameters of the Commonwealth, arbitrators' decisions and unfunded mandates such as GASB 45 (accruing funds for retiree health care costs for fire and police).

Municipalities may invoke Act 47—the Municipalities Financial Recovery Act of 1987—when they meet certain criteria; for example, general fund deficits for over three years, expenditures exceeding revenues for multiple years, a quantifiable decrease in municipal services from the previous year, and others. Deficits may come from one or more situations such as a stagnant or declining real estate base, increased personnel costs, mismanagement, unforeseen events, risky development projects, and tax limitations based on the form of government.

What is necessary to capture the public's attention before the case study municipalities seek Act 47 protection? An easy answer is immediate legislative action; the realistic answer is some mix of legislative action, increased communication, assistance to streamline shared

services, regional tax based sharing, practical cost-centered arbitration awards, citizen awareness of municipal purpose and creative nonprofit participation in municipal costs.

The Pennsylvania Department of Community and Economic Development, Center for Local Government Services in conjunction with the Pennsylvania League of Cities and Municipalities have listened to the pleas of local government officials and asked the Pennsylvania Economy League to conduct case studies of five core eastern Pennsylvania cities as well as other municipalities. This research and analysis identifies the similarities and the differences in the case study municipalities' financial stability

Ultimately, change will involve statewide discussion but first it must be accepted that the current "system" is flawed and that workable remedies, instead of recovery plans, can be achieved to reform the system that propels municipalities into distress.

CHAPTER 2
REVIEW OF MUNICIPAL REVENUE SOURCES, TAXES, FEES,
AND OPERATIONAL SUPPLEMENTS

Historically municipal governments in Pennsylvania, as in most other states, have relied on real estate taxes to provide revenue for the provision of municipal operations and services. Principally through the passage of Act 511 of 1965—The Local Tax Enabling Act—a municipality could supplement the municipal real estate tax with:

- Earned Income Tax (EIT)—based upon residents’ earned income and net profits;
- Mercantile and Business Privilege Tax—based on the gross sales of merchants, business and professional services;
- Real Estate Transfer—a tax shared with the county on the transfer of real estate;
- Per capita tax—a tax on each resident subject to some conditions;
- Occupational and occupation taxes—tax based upon a person’s occupation supplement
- Local Services Tax—a new tax replacing the Occupational Privilege Tax, levied on persons that work within a municipality regardless of residency.

(For the most part, the subjects of taxation of Act 511 taxes as well as tax rates are subject to specific limits.)

Home Rule municipalities (municipalities which chose a charter form of municipal government) may levy EIT and real estate transfer taxes with rates higher than those allowed by statute. For the real estate tax, certain millage limits may not be exceeded unless the municipality is a home rule entity or prior court approval is obtained.

As both the cost of municipal services and the type of services increased, municipal governments began to charge specific fees for certain public services and permits. Penalties such as parking tickets and ordinance violations became a larger portion of funding resources. Grants and other forms of intergovernmental revenue from the federal and state government were increasingly relied upon to replace and supplement local tax effort.

State assistance to maintain and improve roads through the allocation of the liquid fuels program as well as state aid to meet pension obligations has become especially critical to the municipal balance sheet.

From an expenditure perspective, municipal costs for local police, paid fire departments, and street/road maintenance were historically the most important areas of service delivery and the largest proportion of expenditures. Police and fire protection is the most costly aspect of municipal service because they are generally a 24-hour, seven day coverage system; compensation generally reflects the fact that the level of training and possible danger to the respective police officer and fire fighter is greater than for most other municipal employees; labor contracts for these employees can be subject to Act 111 of 1968, which mandates binding arbitration and prohibits strikes in the event of a failure to agree under a collective bargaining process.

Street maintenance and improvements are not round the clock coverage, except in severe weather conditions, and the level of training and/or hazardous duty are less than for police and firefighters. Further, most major road construction or rehabilitation is generally contracted out to third party construction entities. Public Works employees are also covered by state law, Act 195 of 1970 which permits strikes by union personnel within a defined set of parameters.

Generally speaking, water and/or sewer services, if such services are not provided by a utility, are provided by the municipality or a municipal authority created for such a purpose. In the past municipal tax dollars may have been used to meet the costs of these utility type operations. In the current fiscal system, separate fees are almost always charged by the municipality or authority to provide the service. Furthermore, from an accounting perspective, if the system is a municipal operation, the revenue and expenditures are generally recorded in a separate municipal accounting fund, not in the municipality's General Fund.

The refuse collection function has also followed the pattern of generally being paid by separate fees charged to municipal residents or performed entirely by nongovernmental third party contractors. The use of tax dollars to pay for refuse collection is quite limited. Also, the accounting for both the revenue and expenditure side of this service is more frequently recorded in the General Fund than are water and sewer operations.

Utility payments or transfers in amounts greater than simple reimbursement for costs incurred in a municipalities' General Fund are becoming more common. Municipalities consider these revenue flows to be "return on investments" which can be used by the municipality to meet other non utility operational expenditures in the General Fund. In reality these "return on

investments” become an operational supplement to the non utility functions of the municipal government.

Perhaps the most important area of financial interest in operational supplements is the use of debt and debt related instruments in municipal finance. Under Pennsylvania law, debt is to be used for specific projects, primarily capital improvements, rather than to finance operations. In addition, debt may be used to fund unfunded accrued pension liability—a replacement of pension debt with specific bond debt. (In general, given appropriate market conditions, it is believed that the interest rate spread on return favors the exchange of the two types of debt.) However, in recent years the practice of borrowing to generate debt proceeds to meet operational expenditures has become more common. Further, some municipalities have engaged in various forms of financial derivative transactions and/or forward bond contracts, the proceeds or “savings” of which are provided up front and used for operations, most frequently into the General Fund. Finally, it is not uncommon for municipalities to refinance their existing debt and take the overall cash flow savings in the upfront period; the goal is to pay for operational expenditures when there is not sufficient tax or other revenue. From an accounting perspective most of these debt transactions are reported in the General Fund and/or debt service.

One of the primary goals of this study is to isolate and determine among the case study municipalities the extent to which these various Operational Supplements have been used over the 2002 through 2008 period. Operational Supplements are defined as those items which are either classified as revenue or from other sources of funds and are unique in that they are:

- of a one-time nature and/or;
- an ongoing funding stream but are not directly related to meeting expenditures of normal operations and/or;
- derived from the sale of an asset and/or;
- derived from the incurring of a liability.

They include:

- structured lease and sale of a large municipal asset;
- transfers from other funds (in particular enterprise (water, sewer, light) utility funds other than for true municipal cost reimbursement);
- incurring or restructuring of debt, the proceeds of which are used for operations;

- use of financial derivatives, the cash proceeds then are used to fund operations; and
- restructuring of debt primarily to take cash flow savings in the current period(s) in order to meet increases in operational costs.

CHAPTER 3 CITY OF READING

Reading City has a population of about 80,769 persons (2007 Census estimate) and is the fifth largest city in Pennsylvania. Northwest of Philadelphia, southeast of Allentown, northeast of Lancaster, Reading is the county seat of Berks County. Its population peaked in 1930 at 111,000 persons, and was at its lowest point in 1990 (78,000 persons). The City has a varied racial population: in 2000 people identifying themselves as white made up 48 percent of the population, African American were 12 percent, and Hispanic of any race, 37 percent. As Reading's population has increased, so has its diversity. In 1990, 78 percent of the people identified themselves as white, yet ten years later only 48 percent similarly identified themselves. During the same timeframe, the African American population increased from almost ten percent to just over 12 percent and the Hispanic population of all races more than doubled from 14,000 persons to 30,300. In August, 2008 the U.S. Census Bureau reported Reading had the highest poverty level in the Commonwealth for similarly sized cities with an estimated 35 percent of its population earning less than \$21,000 per year.

City Government

Reading City has a home rule charter form of government, which in addition to establishing the organizational structure and procedures for the City, also defines the limits and ways revenues may be obtained. The Mayor, as chief executive officer, has the power to appoint—with the confirmation of City Council—all department heads and the City's Managing Director.

On May 30, 2008, second term Mayor Thomas McMahon presented "Commitment to the Future of Reading, Plan of Action" to Reading City Council and the public. The Mayor's presentation affirmed the City's commitment to provide public safety (police, fire, EMS), community improvement (zoning, codes, public works, planning, and community development), and other administrative requirements (legal, human resources and finances). The plan also presented Reading's fiscal future and necessary council actions. The Reading Plan suggests a menu of potential remedies on the local level:

- a countywide reassessment;
- consolidation or regionalization of police, fire, water and sewer; and
- a regional asset district funded by new revenues on a regional basis.

At the state level, the plan suggests legislation:

- to provide a local option sales tax;
- to provide a liquor by the drink tax;
- to reallocate the Johnstown flood tax revenue;
- to budget an annual appropriation to compensate for the impact of nonprofits; and
- to modify the state requirement to provide public safety services.

On October 1, 2008, Reading’s Managing Director, Ryan Hottenstein presented a \$71.5 million budget for 2009 with a 22.9 percent tax increase. The 2009 budget presentation summarizes revenues and expenses from 2003 through 2007, the 2008 budget and estimates the budgets for 2009 to 2013. The 2008 balanced budget of \$60 million grows to almost \$100 million in expenditures by 2013. Budgeted one time transactions that balance the current City budget, for example, selling a city owned lake to Berks County in 2008, cannot be used again in the future.

The Revenue Experience of Reading City

Tax revenue sources for Pennsylvania cities are largely composed of property taxes and earned income taxes. Both taxes rely on a taxable base of value; for property, it is the assessed values of properties; for the earned income tax, the base is mainly the earnings of wage earners who reside—not just work—in the city. As any tax base increases in size, the revenue to the city increases without official action. If the tax base is stagnant or declining, tax revenue does not “naturally” grow. Governments can raise the tax millage rates on property to increase revenue and may be able (under certain circumstances) to raise the earned income tax rate percentage. (See Table 1.)

Table 1
 CITY OF READING
Real Estate Taxes, Assessed Values, Millage Rates
 2003 - 2007 Actual, 2008 Budget

Year	Assessment	Millage	Taxes Levied	Taxes Collected	Change					
					Assessed Valuation		Tax Rate		Taxes Collected	
					\$	%	Mills	%	\$	%
2003	\$1,454,352,480	10.30	\$14,979,831	\$14,632,135	-	-	-	-	-	-
2004	1,444,301,900	10.30	14,876,310	14,629,341	-10,050,580	-0.69	-	-	-2,794	<-0.1
2005	1,451,953,400	10.30	14,955,120	14,995,914	7,651,500	0.53	-	-	366,573	2.5
2006	1,448,560,900	10.40	15,065,033	15,154,040	-3,392,500	-0.23	0.10	1.0	158,126	1.1
2007	1,464,362,200	10.90	15,961,548	15,384,219	15,801,300	1.09	0.50	4.8	230,179	1.5
2008 Budget	1,455,654,200	10.90	15,866,631	15,430,579	-8,708,000	-0.59	-	-	46,360	0.3
Change										
2003-2007										
\$	\$10,009,720	0.60	\$981,717	\$752,084	-	-	-	-	-	-
%	0.7%	5.8%	6.6%	5.1%	-	-	-	-	-	-

Note: Taxes Collected included General Fund (City Unaudited), Debt Service Fund and Recreation Fund (Audited)

The last countywide reassessment for Berks County was in 1994; the countywide common level ratio for assessments to market value is 65 percent. In 2007, the Reading City ratio of assessed values to market values was 109.1 percent, meaning that the taxed assessed values in Reading may be higher than the actual market values of the property. During the period 2003 to 2008, market values rose by 11.4 percent while Reading City’s assessed valuations grew by one-tenth of one percent. Since 2003, the City’s millage rate increased by 5.8 percent. The lack of growth in assessed property values resulted in a net 5.5 percent increase in the taxes collected. In addition, as the assessed valuations remain higher than the market values, assessment growth will be much less than market growth for the near future. **A countywide reassessment would narrow the City’s ratio of assessed to market value, but may also capture the growth in property values experienced in the City since the 1994 reassessment.** (See Table 2.)

Table 2
 CITY OF READING
Market to Assessed Valuations
 2003 - 2007

<u>Year</u>	<u>Market Value</u>	<u>Assessed Values Ratio to Market Values</u>
2003	\$1,174,396,400	123.9
2004	1,209,538,800	119.4
2005	1,206,414,200	119.4
2006	1,309,931,000	109.1
2007	1,308,441,200	109.1
Change 2003-2007		
\$	\$134,044,800	
%		11.4%

SOURCE: State Tax Equalization Board.

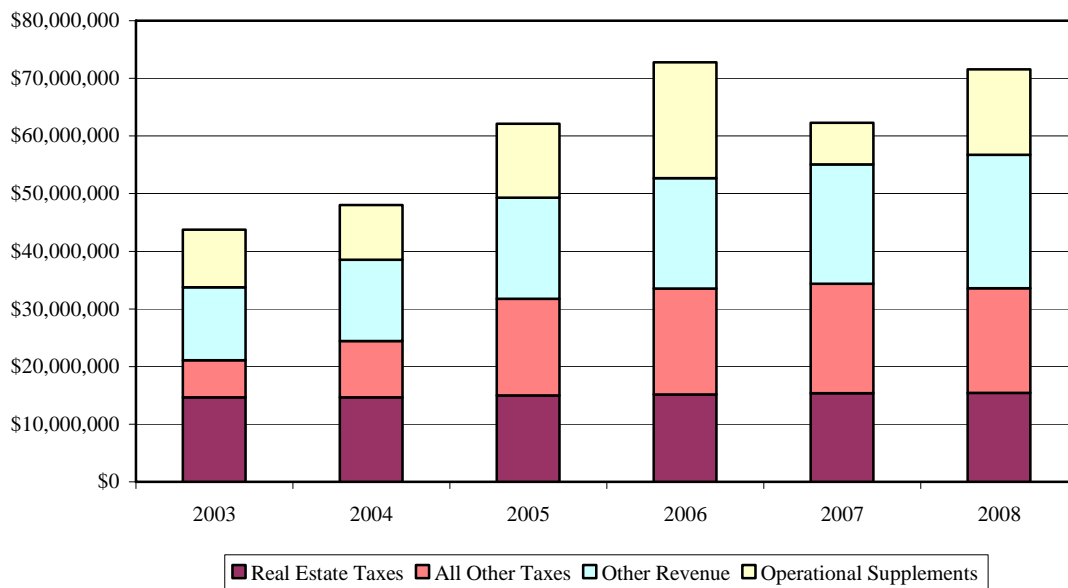
Further increases in the tax millage rate may also be counter productive. In 2005, Reading City property taxpayers paid a per capita property tax of \$185 compared to \$86 paid per capita average of the county’s other municipalities. On the earned income tax revenue side, City residents pay a higher percentage of their income compared to most other county municipalities, as a result, the per capita earned income tax paid in 2005 by city residents was \$107 compared to the county per capita of \$81, or a rate of 1.3 times more than non-city residents in Berks County. (See Table 3.)

Table 3
 CITY OF READING
Earned Income Tax
 2002 to 2007

<u>Year</u>	<u>% Rate</u>	<u>Total EIT</u>	<u>Change</u>	
			<u>\$</u>	<u>%</u>
2002	0.5	\$3,847,321	-	
2003	1.0	3,394,898	-452,423	-11.8
2004	1.2	5,492,391	2,097,493	61.8
2005	1.2	8,714,240	3,221,849	58.7
2006	1.2	8,058,263	-655,977	-7.5
2007	1.2	8,850,005	791,742	9.8
Change 2002-2007	0.7	\$5,002,684	130.0%	

When the City’s general fund expenditures in 1998 totaled \$39.3 million, the property tax provided 34.4 percent or \$13.5 million of the annual budget. By 2008, the City’s general fund budget was \$71.6 million and the property tax provided \$14.3 million or 20 percent of the budget (with \$800,000 in additional property tax funds). If Reading was to maintain the same percentage property tax contribution to the general fund budget in 2008 as it did in 1998, it would have needed to increase the real estate tax rate by 9.6 mills, an 88 percent increase in property taxes. However, the City’s home rule charter limits property tax increases to no more than five percent per year or a maximum compounded increase of 27 percent over five years. Property tax revenues simply do not support Reading’s general fund budget to the extent they did in prior years. (See Graph 1.)

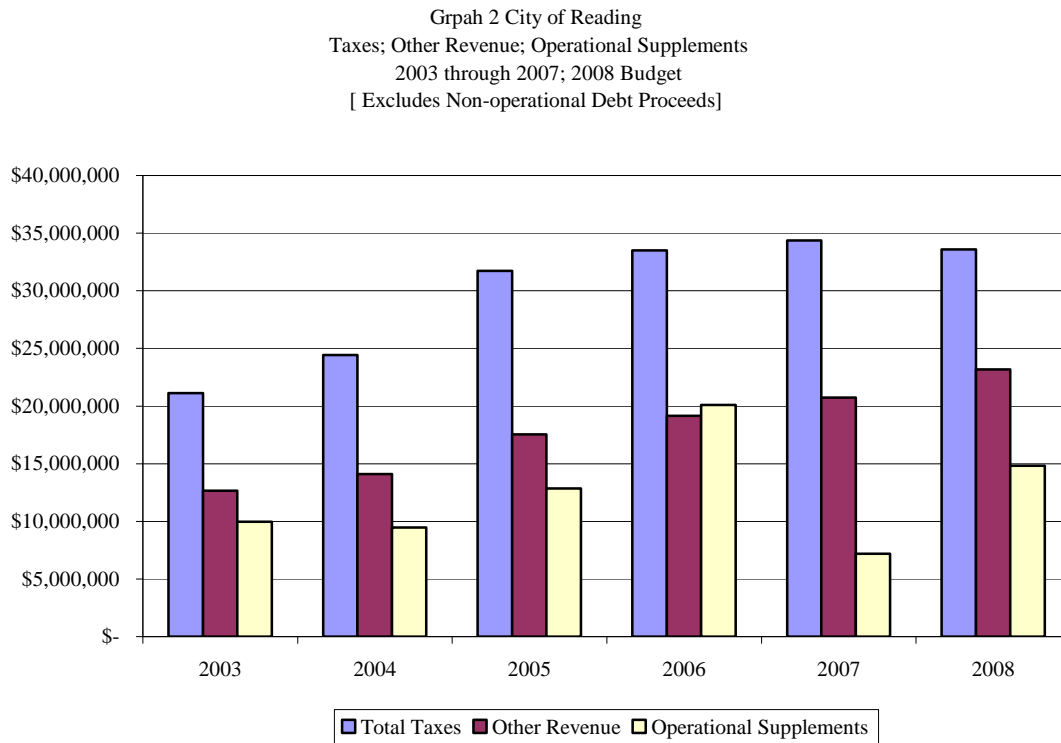
Graph 1 City of Reading
Revenue Components
2003 through 2007; 2008 Budget
[Excluding Non-operational Debt]



In the last ten years, the City’s property tax rate increased by 5.8 percent. From 1998 through 2005, real estate millage was 10.3; in 2006, it increased to 10.4; for 2007 and 2008 the rate was 10.9 mills. During the same period, the real estate transfer tax was increased to five percent—the highest rate in the Commonwealth—and the earned income tax was raised by 0.7 percent to 1.2 percent. Reading took full advantage of the Emergency Services/Local Services

tax that the Governor signed into law in 2004. The City has also sought increased revenues from sources other than taxes.

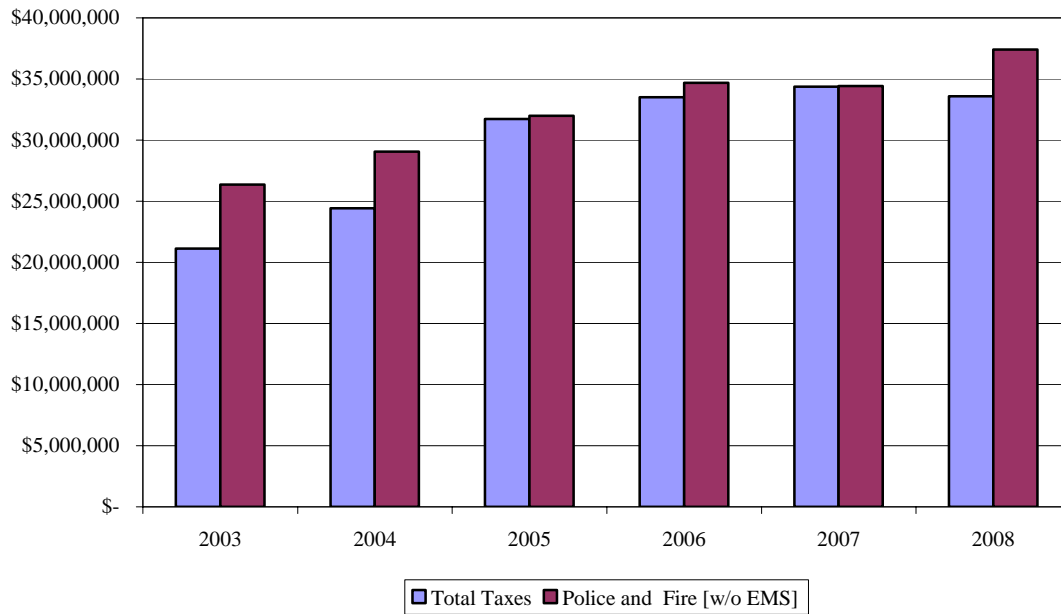
Graph 2 shows the growth in taxes, other revenue sources, and operational supplements from 2003 to 2008.



The Expenditure Experience of Reading City

While the growth in revenue and the mix of revenue sources changed in the review period, operating costs further increased expenditures. A review of the operational categories tells the story. In round numbers, public safety personnel expenditures grew by \$12 million dollars from 2003 through 2007, while personnel headcount remained fairly constant. (Public safety salaries increased by 28 percent, employee benefits rose by 81 percent, and pension costs were up 176 percent.) When total taxes are compared to public safety expenditures in 2007, taxes collected exceeded expenditures by \$300,000; in prior years, **these same expenditures exceeded taxes collected.** (Prior to 2005, EMS expenditures were accounted for in a separate fund.) The following graph provides a visual comparison of total taxes to police and fire expenditures. (See Graph 3.)

Graph 3 City of Reading
 Police and Fire Expenditures Compared to Total Taxes
 2003 through 2007; 2008 Budget



During the same 2003 to 2007 timeframe, community improvement personnel expenditures grew by \$1.3 million as reflected by a 25.5 percent increase in salaries, 41 percent in benefits, and 745 percent increase for pensions. Personnel costs for elected officials increased 43 percent for salaries, 13 percent for benefits, and 923 percent for pensions for a total increase of \$173,000. Administrative support personnel expenditures were up slightly over one million dollars due to salary increases of 29 percent; 52 percent for benefits; and 1,114 percent for pensions. Perhaps the most telling fact about these increases is that during the review period the total number of all full time employees in the City of Reading increased by three, from 710 to 713 employees. A summary of total expenditures for the City by type of expenditure is presented in Graph 4. Actual and budgeted dollars are provided in Table 4.

Graph 4 City of Reading
Expenditure Components
2003 through 2007; 2008 Budget
[Excluding Non-operational Debt Uses]

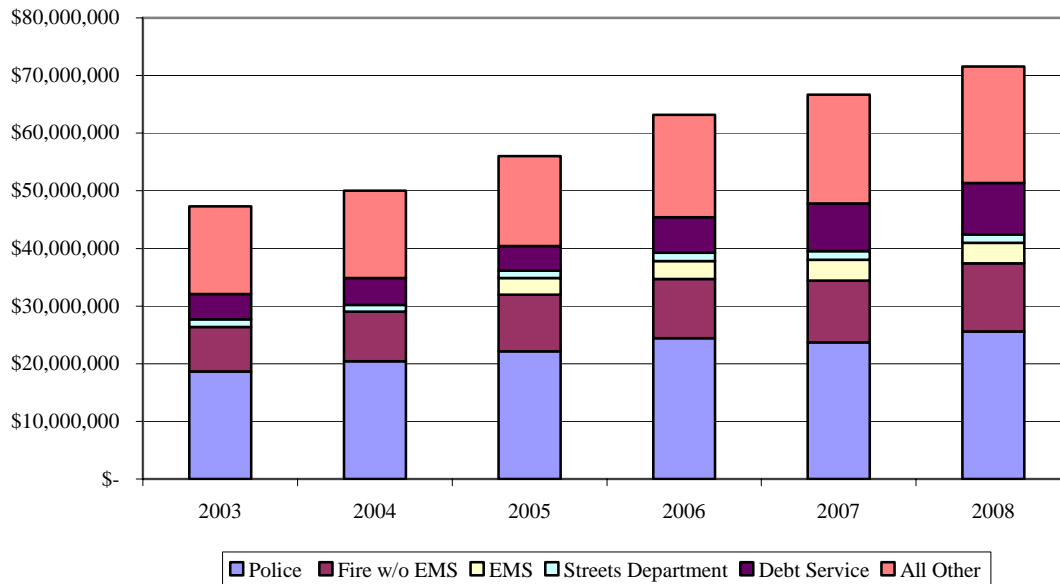


Table 4
CITY OF READING
Actual and Budgeted Expenditures
2003 to 2008

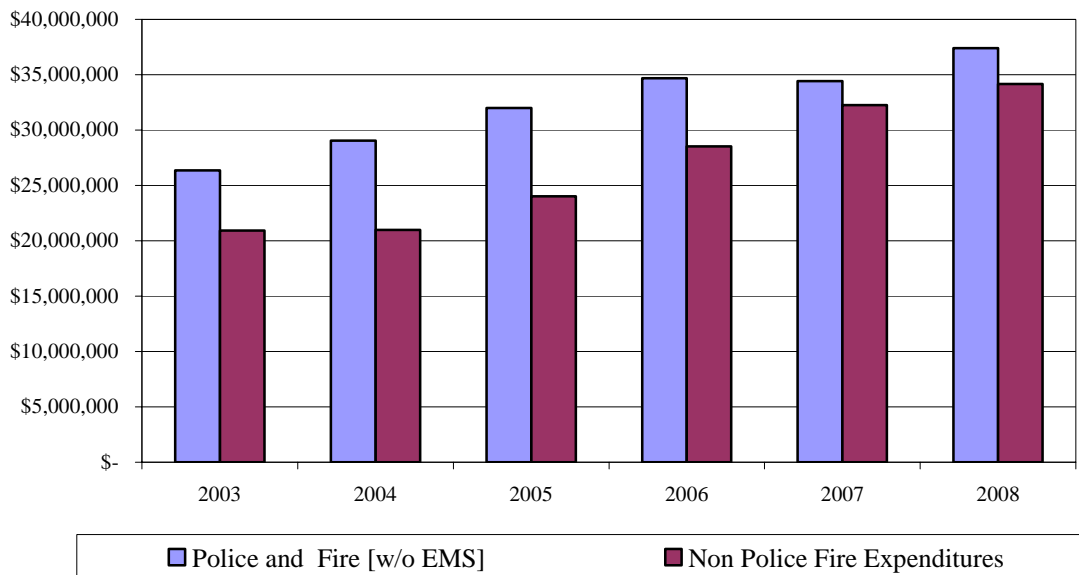
<u>Expenditures</u>	<u>2003 Actual</u>	<u>2004 Actual</u>	<u>2005 Actual</u>	<u>2006 Actual</u>	<u>2007 Actual</u>	<u>2008 Budget</u>
Police	\$18,639,323	\$20,430,513	\$22,126,102	\$24,447,227	\$23,715,580	\$25,573,648
Fire w/o EMS	7,720,486	8,627,777	9,864,805	10,232,975	10,702,747	11,824,670
EMS	-	-	2,889,237	3,128,181	3,585,381	3,587,176
Streets Department	1,363,996	1,164,018	1,260,730	1,420,290	1,529,304	1,406,879
Debt Service	4,364,197	4,662,681	4,289,264	6,190,621	8,251,595	8,934,529
All Other	<u>15,200,566</u>	<u>15,146,389</u>	<u>15,579,909</u>	<u>17,785,574</u>	<u>18,879,432</u>	<u>20,227,243</u>
Total Expenditures	\$47,288,568	\$50,031,378	\$56,010,047	\$63,204,868	\$66,664,039	\$71,554,145

Given the revenue constraints and expenditure growth, the yearly question for the City’s administration goes beyond how the City of Reading will control costs or increase revenues. The annual question is: What drives these significant City operating increases when there is no increase in the number of employees? The short answer is: employee contract arbitration awards,

skyrocketing health care costs, and the costs of maintaining fully funded defined benefit pension plans.

Most citizens would agree that the core mission of a city government is to provide public safety (“safe”) and infrastructure (“clean”). “Clean and safe” is the number one objective for every city mayor and this objective is expensive. Expenditures each year for police and fire protection exceed the total of all other expenditures. (See Graph 5.)

Graph 5 City of Reading
 Police and Fire Compared To All Other Expenditures
 2003 through 2007; 2008 Budget
 [excluding non operational debt uses]



Operational Supplements

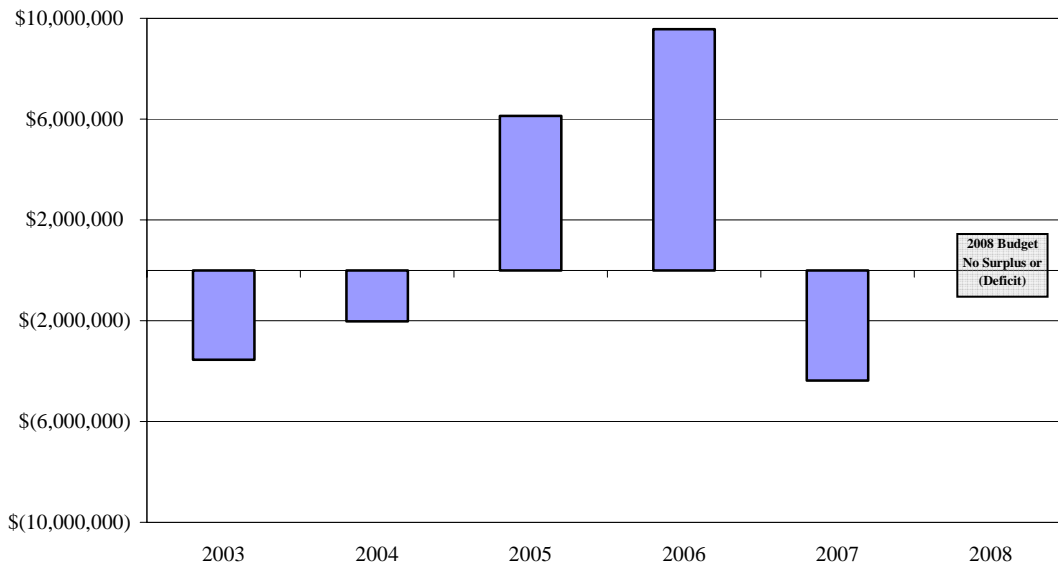
Total taxes collected do not pay for police and fire expenditures, so the City has the task of finding the additional funds to fully pay these operating costs, as well as all other operating expenses of the City.

What other services does Reading provide that may be outside the core mission, but add to the expenses that must be covered by revenues? Two City service cost centers that could be transferred to Berks County are the library (annual cost of \$1.4 million with income of \$900,000) and the 911 dispatch center. Are there other operating costs that can be better controlled? An

analysis of a centralized or group fuel purchase for vehicles is already underway with the school district and the county. The City is also analyzing its electricity usage for street lights, converting to LED traffic controls to offset some of the projected increased electric costs in 2010. Reading does not provide garbage service.

Though Reading has experienced budget surpluses in 2005 and 2006 largely as a result of the sale of a city owned lake and other financing options, its future is not as optimistic. The 2008 budget strives for a no surplus/deficit outcome, but deteriorating economic conditions make that less likely. The 2003-2007 history of surplus of deficit is depicted in Graph 6.

Graph 6 City of Reading
 Surplus (Deficit)
 2003 through 2007; 2008 Budget
 [Excluding Non-operational Debt Sources and Uses]



In a radio interview on March 11, 2008, Mayor McMahon foretold the financial crisis that would befall Reading later in 2008 when he said the City was fortunate to have a surplus at the end of 2006 as a result of some “one-time” occurrences. The Mayor reiterated that the real estate millage rate had been nearly the same since the early 1990’s but that the available revenues have only increased by the size of the millage increase because of a growing number of tax exempt properties and decreases in the assessed valuation base. He said the worst case and least likely scenario going forward would be to cut police and fire, given the taxpayer expected support of the “clean and safe” mission of the City. A continued reliance on one time revenues

every year is the most likely occurrence. Graph 7 presents the “one-time” occurrences that have bridged the shortfall between revenues and operating costs for Reading since 2003. (See Table 5 for the actual dollar amounts.)

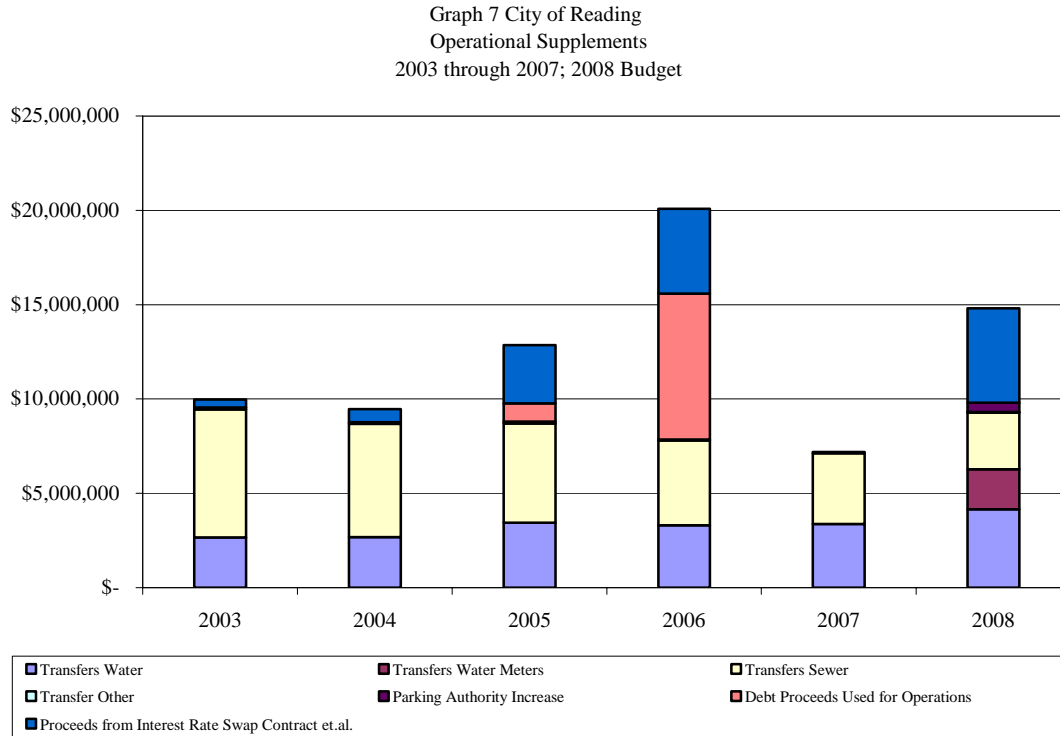


Table 5
CITY OF READING
Operational Supplements
2003 to 2008 Budget

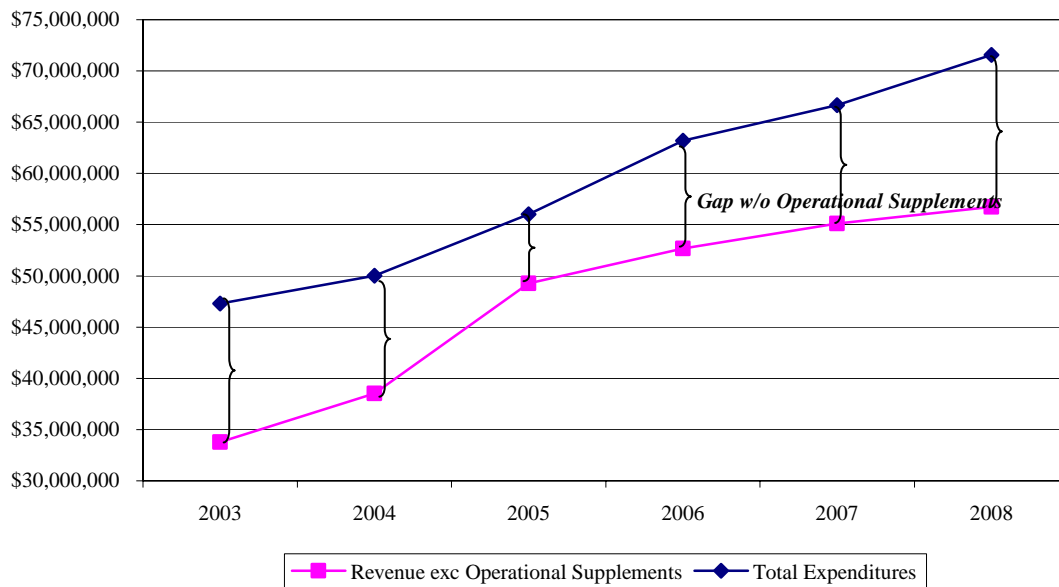
<u>Operational Supplements</u>	2003 <u>Actual</u>	2004 <u>Actual</u>	2005 <u>Actual</u>	2006 <u>Actual</u>	Draft Audit 2007 <u>Actual</u>	2008 <u>Budget</u>
Transfers Water	\$2,655,697	\$2,687,024	\$3,449,048	\$3,304,338	\$3,378,313	\$4,150,000
Transfers Water Meters	-	-	-	-	-	2,125,000
Transfers Sewer	6,790,505	6,000,000	5,250,000	4,500,000	3,750,000	3,000,000
Transfer Other	102,549	83,440	99,401	43,940	60,371	35,000
Parking Authority Increase	-	-	971,596	7,740,320	-	500,000
Debt Proceeds Used for Operations	-	-	-	-	-	-
Proceeds from Interest Rate Swap Contract	425,000	700,197	3,091,200	4,500,397	-	5,000,000
Yearly Total Operational Supplements	\$ 9,973,751	\$ 9,470,661	\$12,861,245	\$20,088,995	\$7,188,684	\$14,810,000
Percent of All Other Revenues	29.5	24.6	26.1	38.1	13.0	-

The City has used operational supplements in each budget year during the review period and has used the proceeds to balance the budget, prevent deficits, and to continue to provide services to residents. As a percentage of all other revenues realized by the City for the review

period, these operational supplements range from 13.0 percent in 2007 to 38.1 percent in 2006, for the five year review period, the average was 26.2 percent.

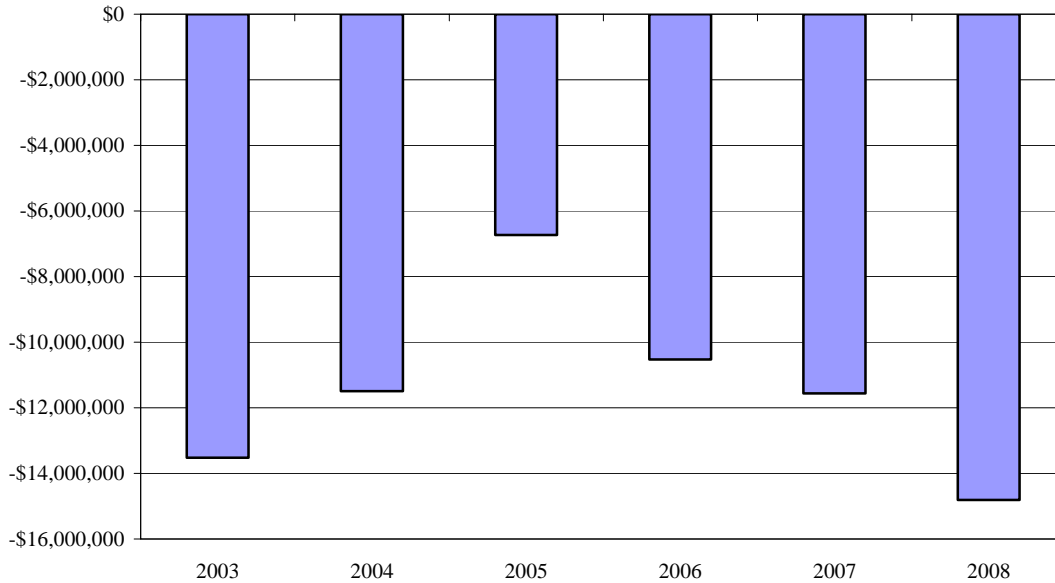
The role of operational supplements in balancing the City’s budget is shown in Graph 8. The gap filled by these supplements has grown since 2005.

Graph 8 City of Reading
 Revenue without Operational Supplements vs. Expenditures
 2003 through 2007; 2008 Budget
 [Excluding Non-Operational Debt Sources and Uses]



Graph 9 presents Reading’s budget history without the effects of operational supplements, that is, revenues generated by taxes and other revenues and the expenditures required by city operations. A continued pattern of deficits were met with the use of operational supplements.

Graph 9 City of Reading
 Deficit without Operational Supplements
 2003 through 2007; 2008 Budget



On Wednesday, October 1, 2008, Reading’s Managing Director, Ryan Hottenstein presented the 2009 city budget on behalf of Mayor McMahon. This would be a \$71.5 million budget with a 22.9 percent real estate tax increase that follows through on the plan unveiled in May. At that time, a 50 percent property tax increase was forecast to close the gap, but the proposed budget will raise the property tax rate by 2.5 mills, from 10.9 mills to 13.4 mills, generating an estimated additional \$3.2 million levy. However, the City’s home rule charter limits any tax rate hike to no more than five percent or no more than 0.54 mill. The proposed 2009 budget also calls for a 0.3 percentage point rise in the earned-income tax (from 1.2 percent to 1.5 percent) to generate an additional \$2.7 million. The budget requires the Reading Parking Authority to give the city \$5.4 million of its surplus in 2009 and \$1.4 million each year after that. The budget uses savings of \$1.1 million that would be achieved through 35 positions remaining vacant or becoming vacant through retirements. The Mayors’ budget message repeats the phrase “rising costs are outpacing revenue.” Last year Reading used fee hikes and one-time revenue to avoid raising taxes, but the Mayor’s message states, “This approach did not work in 2008 and will not work in 2009.”

Based on the City's plan the "Commitment to the Future of Reading, Plan of Action" the following is required:

- **reduce staff** by 5 percent through attrition; a hiring freeze on open positions is in place along with reassigning tasks to others when a co-worker is absent due to short-term disability (previously, temporary employees were hired);
- **increase the property tax** by 5.5 mills in 2009 - essentially negating the school district property tax decrease Reading property owners received as a result of Act 1 and gaming revenue from slot machines;
- **restructure city debt** to reduce annual costs and extend the years of debt; this is aggregate debt related to other general obligation bonds and pension costs; and
- **sell and lease back** the parking authority with a net return to the City of \$8 million in year one.

Even if the above four action steps are accomplished the combined impact provides positive cash flow for 2008 and 2009 but results in a deficit of \$1.7 million in 2010. The mayor fears that Reading is on the brink of declaring Act 47 status.

CHAPTER 4

CITY OF LANCASTER

Lancaster City has a population of 54,672 persons (2007 Census estimate) and is the County seat and the heart of Pennsylvania Dutch Country, a key tourist area. Lancaster is the eighth largest city in Pennsylvania and has a varied population; in 2000, people identifying themselves as whites were 52 percent of the population, African American were 14 percent, and Hispanic of any race, 31 percent.

City Government

Lancaster City operates under a Mayor/Council form of government with offices of Treasurer and City Controller. The City provides for services including public safety, health, housing, parks, streets and highways, water operations and sewer operations. Shortly after current Mayor Richard Gray took the oath of office in 2006, he led the City of Lancaster through a strategic planning process based on the old African proverb that says “a man who doesn’t know where he wants to go, doesn’t need a map.” The strategic plan’s overall goal is to provide residents and visitors with the ideal urban experience through seven strategic focus areas:

- Arts and Entertainment;
- Customer-Centered Culture;
- Housing;
- Mobility;
- Neighborhoods;
- Public Amenities and Ambience; and
- Retail Sector

The plan defines the direction, cultural norms and expectations for the delivery of City services. Simply stated, the plan promises that City government will do its best to provide residents and visitors with a “clean and safe” Lancaster; the common mantra for all mayors across the Commonwealth. The strategic plan, however, does not include revenues and costs related to achieving the goals of this strategic plan.

The Revenue Experience of Lancaster City

Revenue for Pennsylvania cities is largely composed of property taxes and earned income taxes. Both taxes rely on a taxable base of value; for property, it is the assessed values of properties and for the earned income tax it is the earnings of wage earners that reside—not just work—in the city. As any tax base increases in size, the revenue to the city increases without official action. If the tax base is stagnant or declining, tax revenue does not “naturally” grow; however, governments can raise the tax millage rates on property and may be able (under certain circumstances) to raise the earned income tax rate percentage. For the review period of 2003 to 2008, real estate tax revenues for Lancaster City increased as a result of millage increases by the City and by growth in the City’s assessment base. Together these factors contributed to an increase of 20.1 percent in real estate tax revenue since 2003. Lancaster City commercial valuations make up about 35.3 percent of the City’s tax base while residential accounts for 58.5 percent. Property taxes were raised each year since 2006 providing a 19.7 percent increase for the period 2006 to 2008. While the countywide reassessment in 2005 lowered millage rates that year, real estate tax revenues were up by 2.7 percent in the reassessment year. After the reduction of the tax rate following the reassessment, millages were raised by 8.0 percent in 2006 and by 4.1 percent in 2007. (See Table 1.)

Table 1
CITY OF LANCASTER
Real Estate Taxes, Assessed Values, Millage Rates
2003 - 2007 Actual, 2008 Budget

Year	Assessment	Millage	Taxes Levied	Taxes Collected	Assessed Valuation		Change Tax Rate		Taxes Collected	
					\$	%	Mills	%	\$	%
2003	\$1,775,146,400	8.24	\$14,627,206	\$14,437,430	-	-	-	-	-	-
2004	1,792,205,900	8.24	14,767,777	14,249,976	17,059,500	1.0	-	-	-187,454	-1.3
2005	1,919,622,700	7.67	14,723,506	14,653,387	127,416,800	7.1	-0.6	-6.9	403,411	2.7
2006	1,925,412,200	8.17	15,730,618	15,446,028	5,789,500	0.3	0.5	6.5	792,641	5.4
2007	1,939,205,900	8.82	17,103,796	16,482,433	13,793,700	0.7	0.7	8.0	1,036,405	6.6
2008 Budget	1,908,726,600	9.18	17,522,110	17,341,000	-30,479,300	-1.6	0.4	4.1	858,567	5.0
Change 2003-2007										
\$	\$164,059,500	0.58	2,476,590	\$2,045,003	-	-	-	-	-	-
%	9.2%	7.0%	16.9%	14.2%	-	-	-	-	-	-

Note: Taxes Collected included General Fund (City Unaudited), Debt Service Fund and Recreation Fund (Audited)

Since the last countywide reassessment for Lancaster County was in 2005. The countywide common level ratio for assessments to market value has been 73 percent. In 2007 the Lancaster City ratio was 112 percent, meaning that the taxed assessed values in Lancaster City were higher than the actual market values of the property. Since the reassessment, market values have risen by 12.9 percent while the City’s assessed valuations grew by slightly less than one percent. Since 2003, the City’s tax millage rate has increased by 11.4 percent to raise tax revenue, but the growth in assessed property values created a 20.1 percent increase in the taxes collected.

In addition, as the assessed valuations remain higher than the market values, it is likely that assessment growth will be much less than market growth for the near future. (See Table 2.)

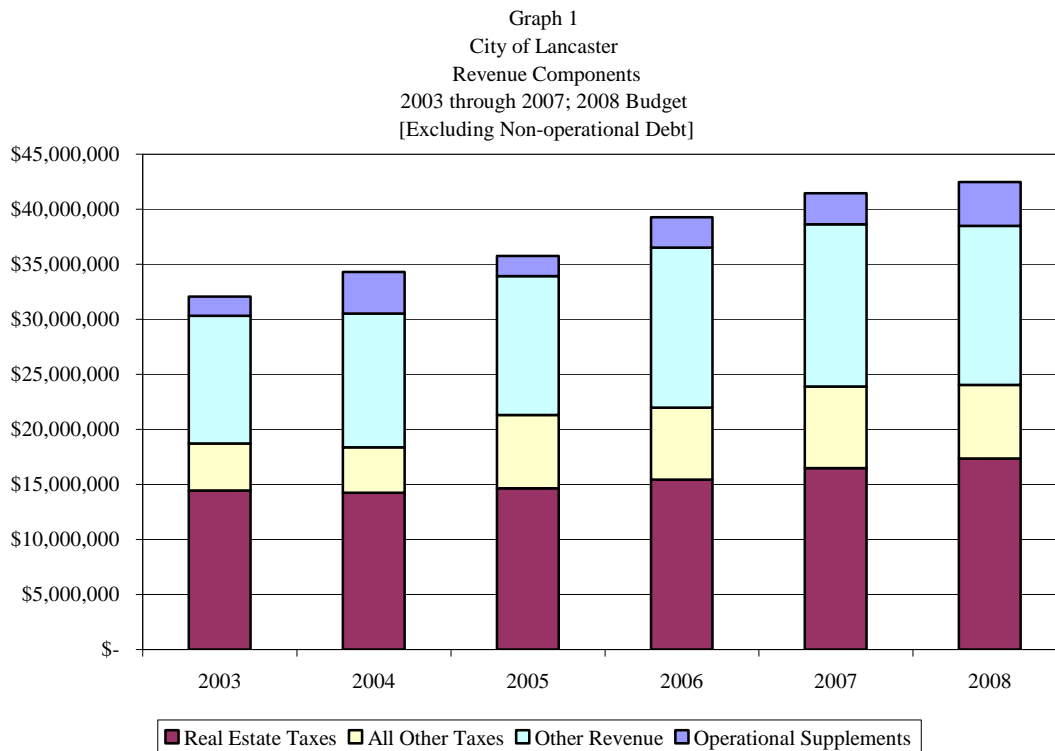
Table 2
CITY OF LANCASTER
Market to Assessed Valuations
2003 - 2007

<u>Year</u>	<u>Market Value</u>	<u>Assessed Values Ratio to Market Values</u>
2003	\$1,359,540,400	123.3
2004	1,434,087,600	116.1
2005	1,436,676,800	125.9
2006	1,606,197,100	112.9
2007	1,621,820,300	112.6
Change		
2003-2007		
\$	\$262,279,900	
%		19.3%

SOURCE: State Tax Equalization Board.

Further increases in the tax millage rate may also be counter productive. In 2005, Lancaster City property taxpayers paid a per capita property tax of \$259 compared to \$75 for the county’s other municipalities, a rate nearly three and a half times as great. On the earned income tax revenue side, City residents pay a slightly higher percentage of their income compared to most other county municipalities. Nonetheless, the per capita earned income tax paid in 2005 by city residents was \$61 compared to \$105 or a rate of three fifths that of non-city residents in Lancaster County.

A portion of the 2007 fund balance was utilized to balance the 2008 budget. While there is a \$2 million annual subsidy to the City’s general fund from the Water and Sewer Authority, the sale of excess capacity from the sewage treatment plant contributed to the \$13.2 million fund balance for 2007. There is no projected property tax increase for 2009 although expenditures will rise. For example, police salaries will increase by 3.5 percent, non-uniformed employee pay will increase by 3.0 percent, and fire department salaries will increase 3.25 percent. A summary of revenue sources is presented in Graph 1.

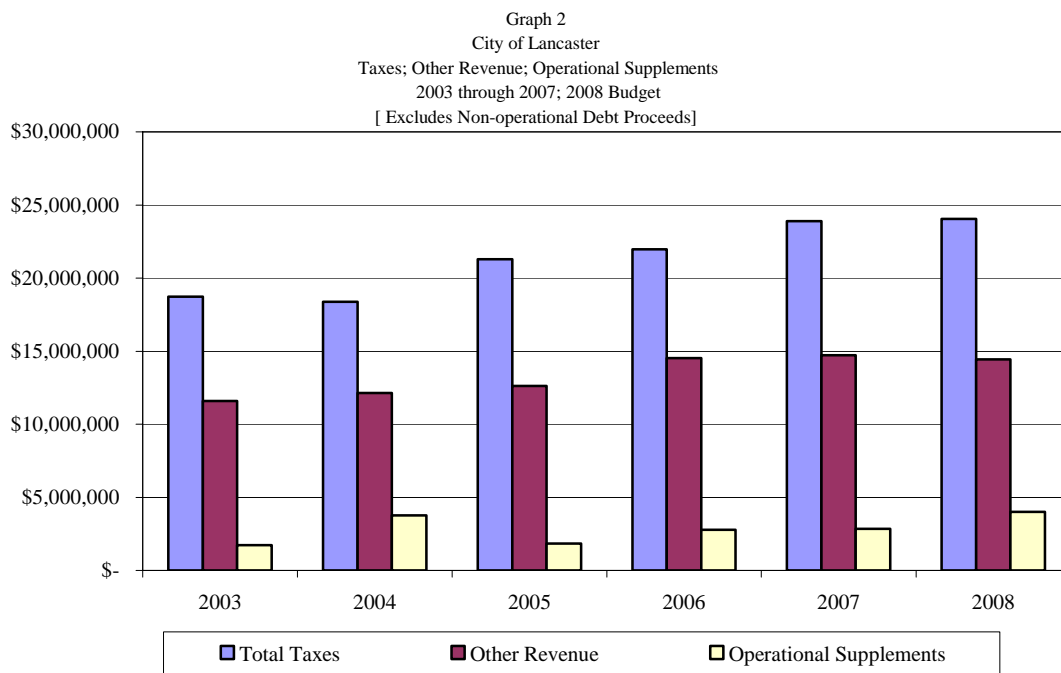


The City of Lancaster sold its real estate tax lien receivables for 2007 and prior years to an independent entity to generate \$800,000 in additional revenue for 2008. Although the City annually turns over \$500,000 to \$600,000 in delinquent real estate taxes to the County for collection, this third-party contract will provide Lancaster City with the funds up front instead of waiting the usual three to five years. Future cash flow from real estate tax delinquents will be lower due to the cash advanced this year. The City would like to achieve the same results from the approximate \$1.475 million in delinquent parking violations. The City does not levy the business privilege and mercantile tax, which may be helpful in attracting and retaining a number of small, privately owned retail and professional storefronts in this attractive tourist area.

The City has a police services agreement with Lancaster Township. This contract generates \$1.4 million annually for 16,000 hours of service time. A cost allocation study verified this charge as appropriate in 2007.

Over \$10 million is received through various fees on an annual basis; however, the last time the fee structure was studied and updated was 1996. The City administration is proposing an omnibus fee ordinance update in the last quarter of 2008.

In addition to tax and fee income, the City has used supplemental revenue to pay for operations each year of the review, ranging from \$1.7 million in 2003 to a budgeted \$4.0 million in 2008. (See Graph 2.)



The Expenditure Experience of Lancaster City

A review of Lancaster’s operating expenditures for the last five years shows that 80 percent of the budget goes to personnel costs, seven percent to debt service, and 13 percent to be used for normal operating expenditures. The City makes an annual contribution to the county library and supports recreation programs and facilities in cooperation with the school district and Lancaster Township. Through the Lancaster Inter-Municipal Committee of thirteen

municipalities, the City participates in a regional approach to planning and zoning. Expenditures are summarized in Graph 3. Actual and Budgeted expenditures are presented in Table 3.

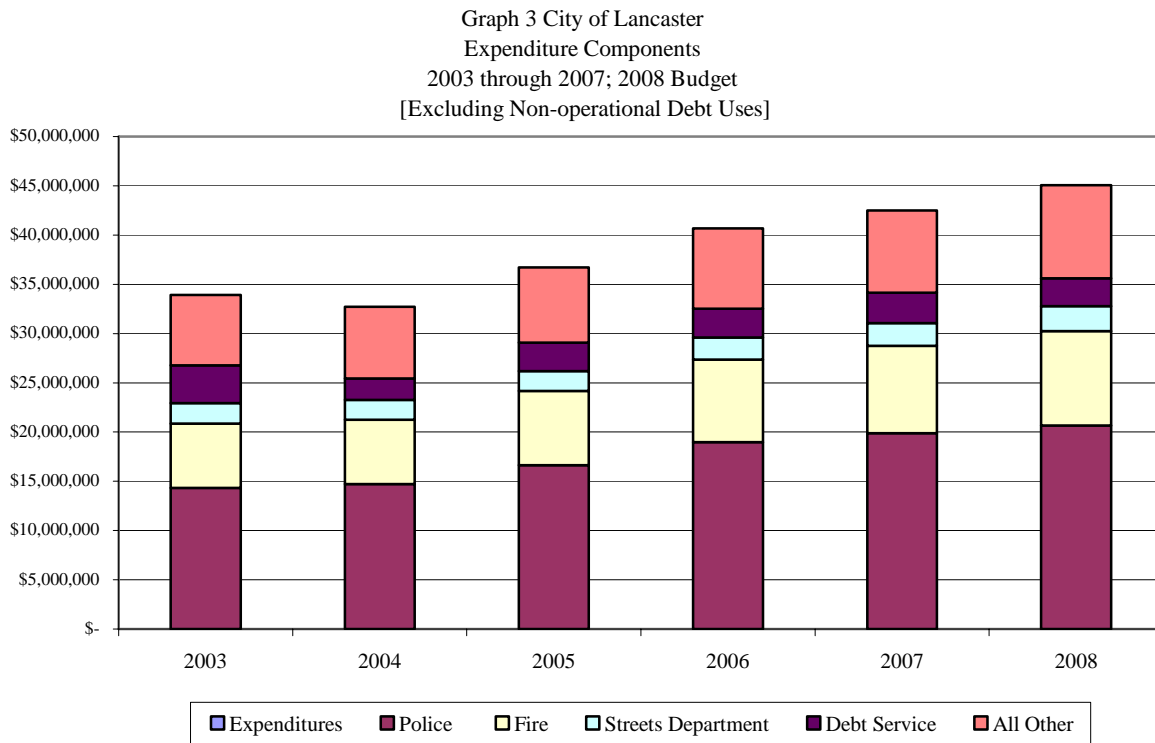


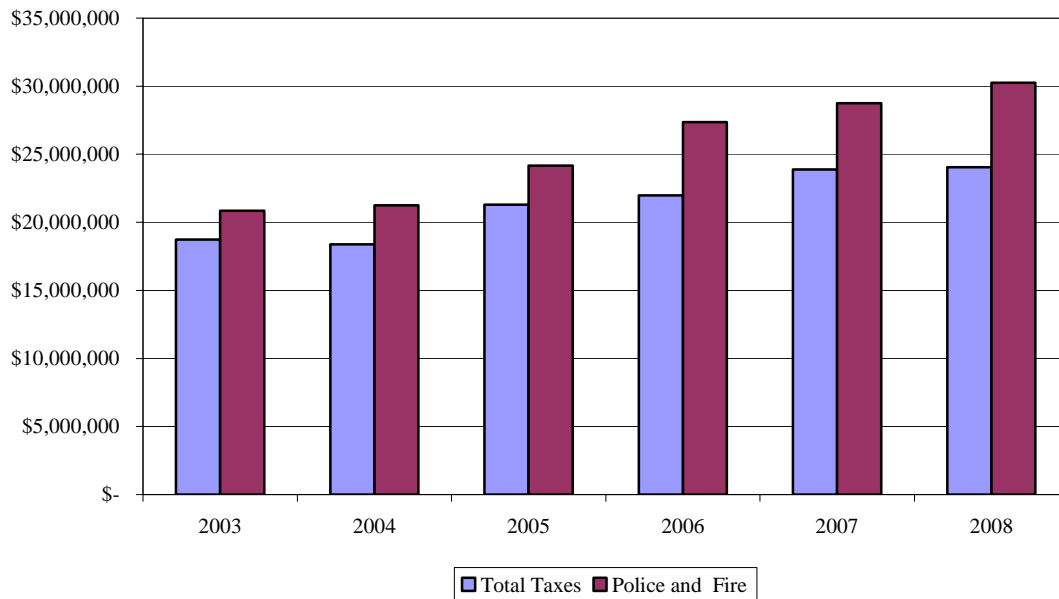
Table 3
CITY OF LANCASTER
Expenditure Components
2003 to 2008 Budget

	2003 <u>Actual</u>	2004 <u>Actual</u>	2005 <u>Actual</u>	2006 <u>Actual</u>	2007 <u>Actual</u>	2008 <u>Budget</u>
<u>Expenditures</u>						
Police	\$14,325,803	\$14,701,400	\$16,648,787	\$18,968,305	\$19,871,095	\$20,665,826
Fire	6,525,663	6,547,169	7,508,078	8,393,347	8,873,386	9,593,922
Streets Department	2,097,380	2,020,754	2,029,071	2,249,198	2,314,828	2,517,880
Debt Service	3,833,893	2,172,383	2,898,319	2,900,236	3,071,601	2,838,539
All Other	<u>7,136,184</u>	<u>7,286,638</u>	<u>7,618,356</u>	<u>8,166,021</u>	<u>8,368,190</u>	<u>9,447,515</u>
Total Expenditures	\$33,918,924	\$32,728,344	\$36,702,611	\$40,677,107	\$42,499,100	\$45,063,681
Police and Fire	\$20,851,466	\$21,248,569	\$24,156,866	\$27,361,651	\$28,744,482	\$30,259,748
Non-Police Fire Exp.	<u>13,067,458</u>	<u>11,479,774</u>	<u>12,545,745</u>	<u>13,315,456</u>	<u>13,754,618</u>	<u>14,803,933</u>
Total Expenditures	\$33,918,924	\$32,728,344	\$36,702,611	\$40,677,107	\$42,499,100	\$45,063,681

Mayor Gray advised his department heads to hold increases to 2.5 percent as they prepared their 2009 budget. It is a difficult task to decrease the rate of expenditure increases when the City has relatively high employee fringe benefit expenditures. The employee health insurance provider has agreed to hold the yearly health care cost increases for 2009 and 2010 to nine percent. Yet, since 2003, the cost of health insurance doubled in cost. The City has three defined benefit pension plans with an assumed annual 8.5 percent rate of growth; the City issued an RFP for pension fund management in 2008.

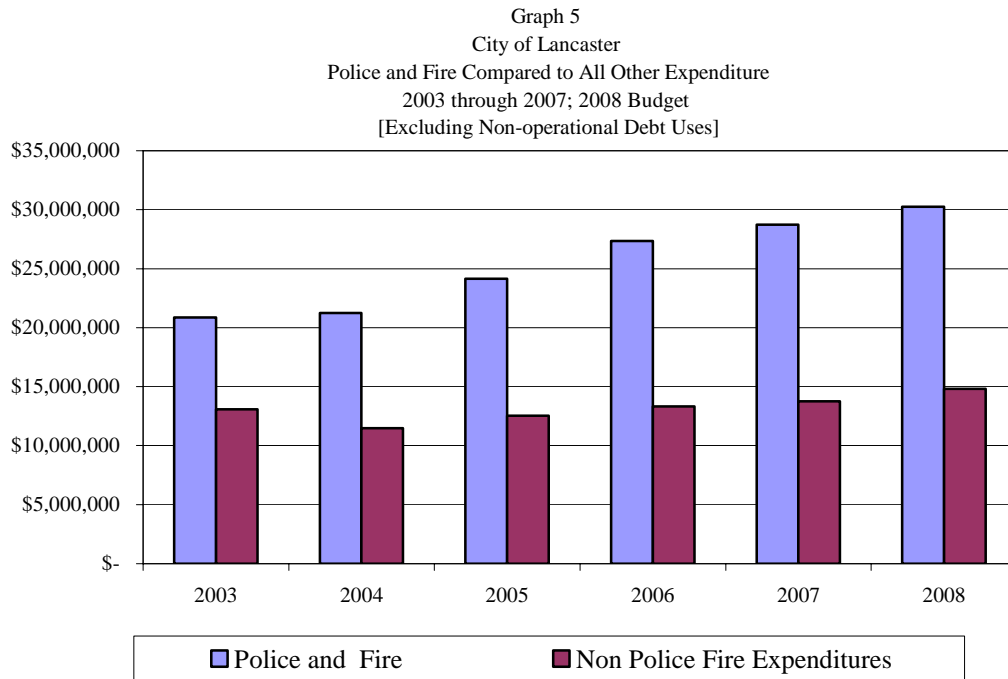
Public Safety expenditures for the police department and fire department lead the annual budget. There is no contractual minimum manning requirement for either department. The City accepted a *PA COPS* grant in 2006 for three years to fund three additional police officers (with the requirement that they be retained for an equal amount of time after the state funding expires). Gun use and drugs are considered the number one crime problem for Lancaster. Note that expenditures for police and fire services exceed total tax revenues for the City. (See Graph 4.)

Graph 4
 City of Lancaster
 Police and Fire Expenditures Compared to Total Taxes
 2003 through 2007; 2008 Budget



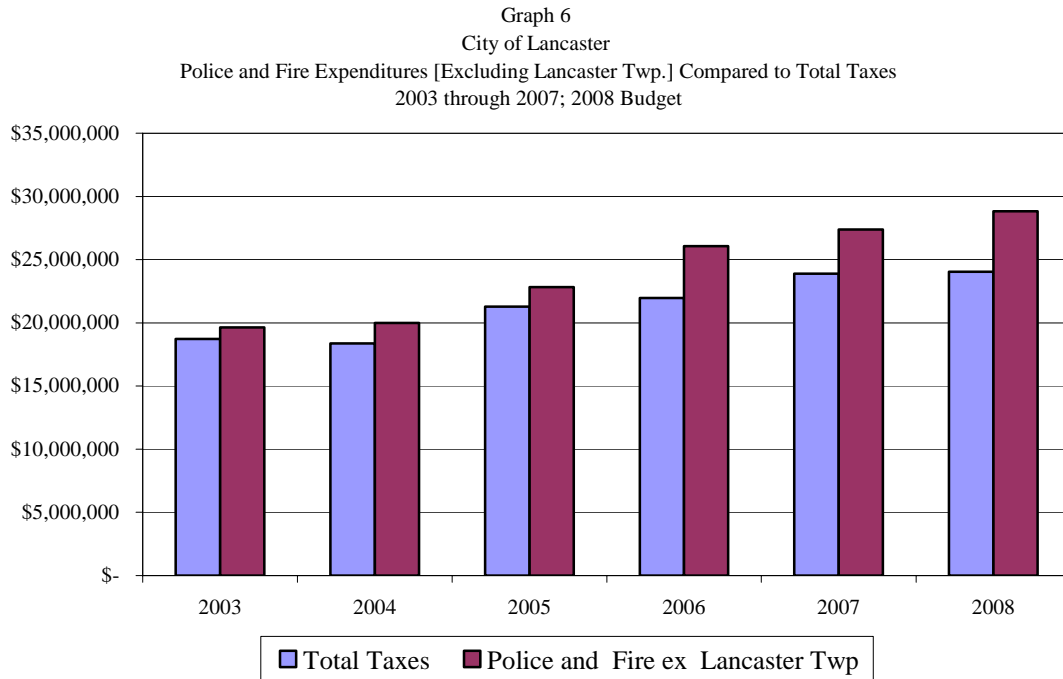
While the City provides police coverage for a neighboring township at a contract price, there is no corresponding joint arrangement for provision of fire services. The City of Lancaster’s fire department currently responds to ambulance calls; however, because it is related

to the annual contribution to the volunteer fire departments, the City’s fire chief is changing the type of call that requires first response. The County provides all 911 services. Together, as seen in Graph 5, combined police and fire expenditures exceed all other City costs combined.



Operational Supplements

Most citizens would agree that the core mission of a city government is to provide public safety (“safe”) and infrastructure (“clean”). “Clean and Safe” is the number one objective for every city mayor and it is expensive. When total taxes are compared to the provision of “Safe”—public safety expenditures since 2003, **these expenditures exceeded total taxes collected.** (See Graph 6.)

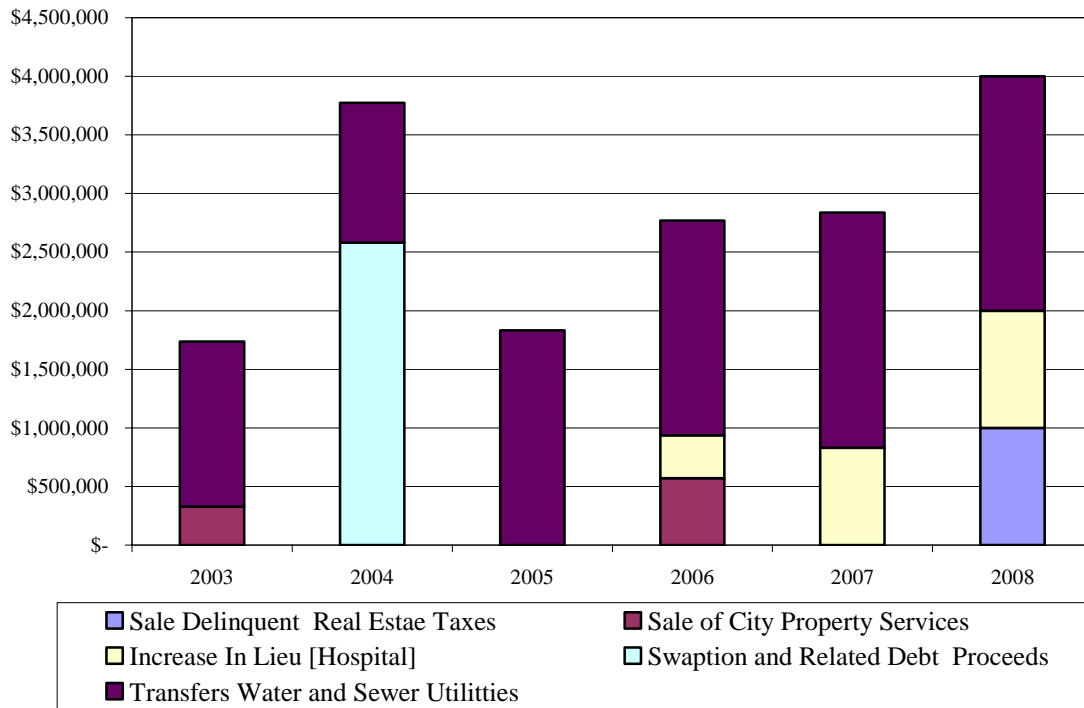


The financial stability of Lancaster has been challenging since the mid-1990s when there were two straight years of deficits due largely to the costs of the City’s self insurance for health care benefits. In response to these shortfalls,

- the City levied a significant tax increase—18 percent in 1996,
- switched to a third party premium based health employee insurance benefit plan, and
- furloughed 17 firefighters.

By 1997 the City had an end of year surplus, but difficulties continued until 2004 when the City initiated a \$2.4 million financing SWAP to cover the structural operating deficit. (A SWAP is an agreement between two parties to exchange future cash flows according to a prearranged formula.) These forms of one-time financing for revenue are considered to be operational supplements to the City’s basic tax and fee sources. The relative role of operational supplements and related debt proceeds are shown in Graph 7.

Graph 7 City of Lancaster
Operational Supplements
2003 through 2007; 2008 Budget



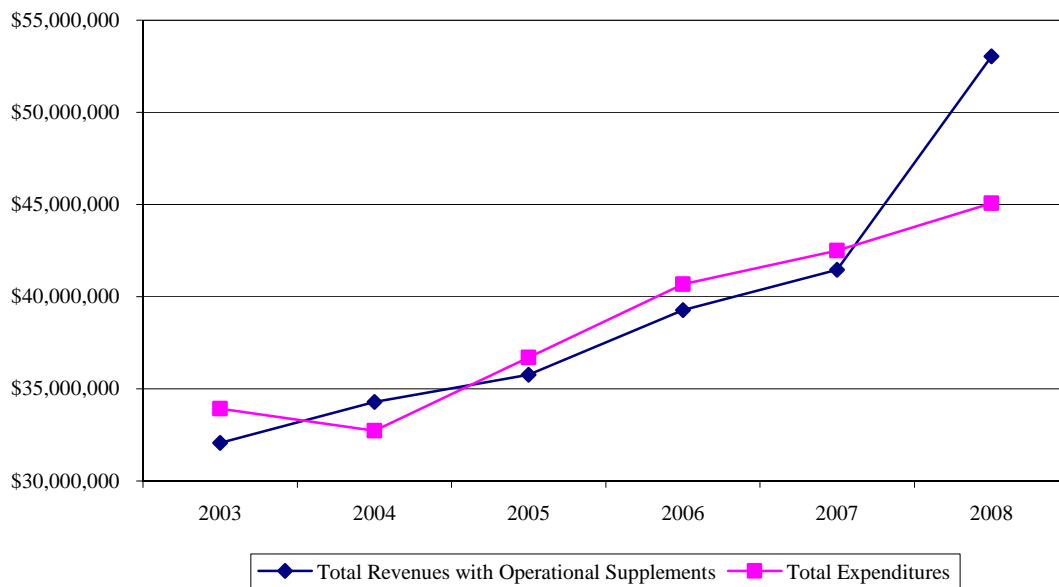
Actual (2003-2007) and budgeted operational supplements are presented in Table 4. Note that these supplements are increasing each budget year. The 2008 budget contains \$4,000,000 of operational supplements.

Table 4
CITY OF LANCASTER
Summary of Operational Supplements
2003 – 2007; 2008 Budget

<u>Operational Supplements</u>	2003 <u>Actual</u>	2004 <u>Actual</u>	2005 <u>Actual</u>	2006 <u>Actual</u>	Draft Audit 2007 <u>Actual</u>	2008 <u>Budget</u>
Sale Delinquent Real Estate Taxes	\$ -	\$ -	\$ -	\$ -	\$ -	\$1,000,000
Sale of City Property Services	327,378	-	-	570,671	1,135	-
Increase In Lieu [Hospital]	-	-	-	366,278	828,786	1,000,000
SWAP and Related Debt Proceeds	-	2,579,822	-	-	-	-
Transfers Water and Sewer Utilities	<u>1,408,311</u>	<u>1,193,634</u>	<u>1,831,127</u>	<u>1,831,127</u>	<u>2,007,128</u>	<u>2,000,000</u>
Total Operational Supplements	\$1,735,689	\$3,773,456	\$1,831,127	\$2,768,076	\$2,837,049	\$4,000,000

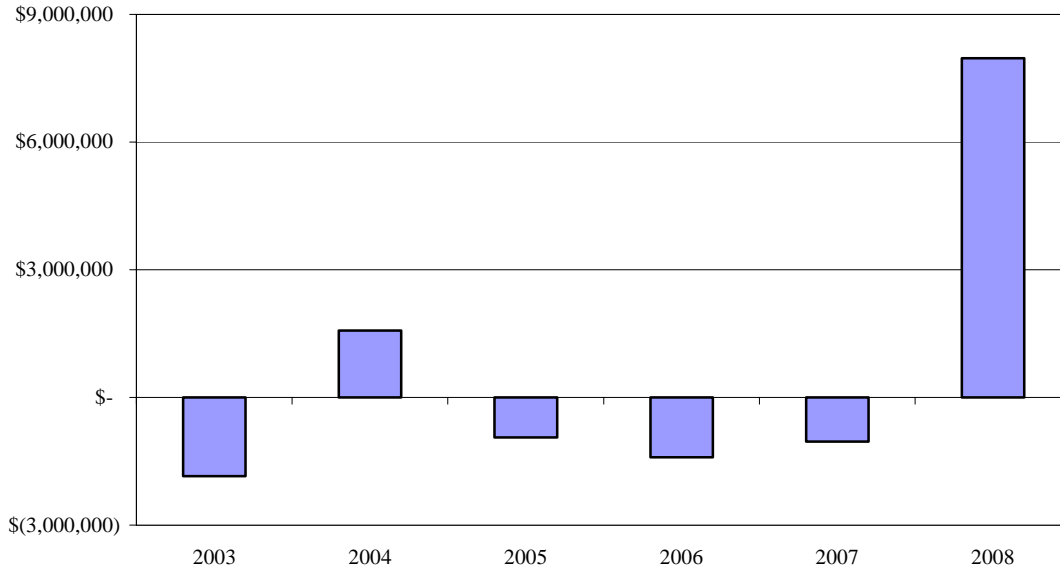
While the dollar amount of the supplemental revenue is not very large on a yearly basis, it has been a stopgap measure against larger deficits in City operations. Even with the additional revenue from this operational financing, Lancaster City has seen expenditures exceed revenues for the period 2003 to 2007, with only one year (2004) showing a surplus of revenue over expenditures after the use of operational revenue supplements. (See Graph 8.)

Graph 8 City of Lancaster
Revenues With Operational Supplements and Expenditures
 2003 through 2007; 2008 Budget
 [Excluding Non-operational Debt Sources and Uses]



As seen in Graph 9, Lancaster City has budgeted in 2008 an almost \$8 million surplus. The weakening economic climate will challenge the City’s ability to meet expenditures.

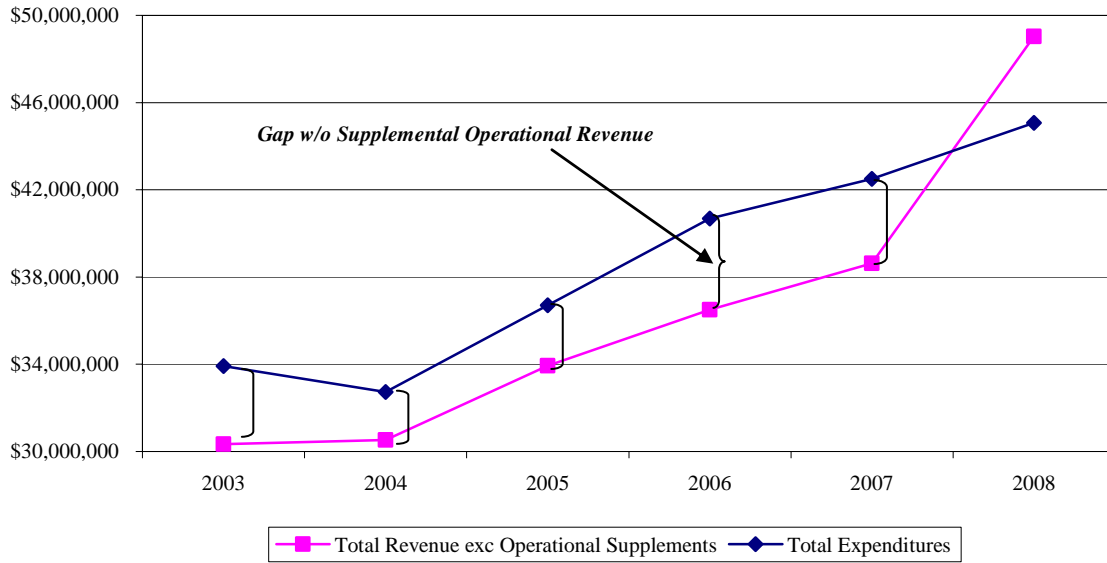
Graph 9
 City of Lancaster
 Surplus (Deficit)
 2003 through 2007; 2008 Budget
Includes All Operational Supplements Funds
 [Excluding Non-operational Debt Sources and Uses]



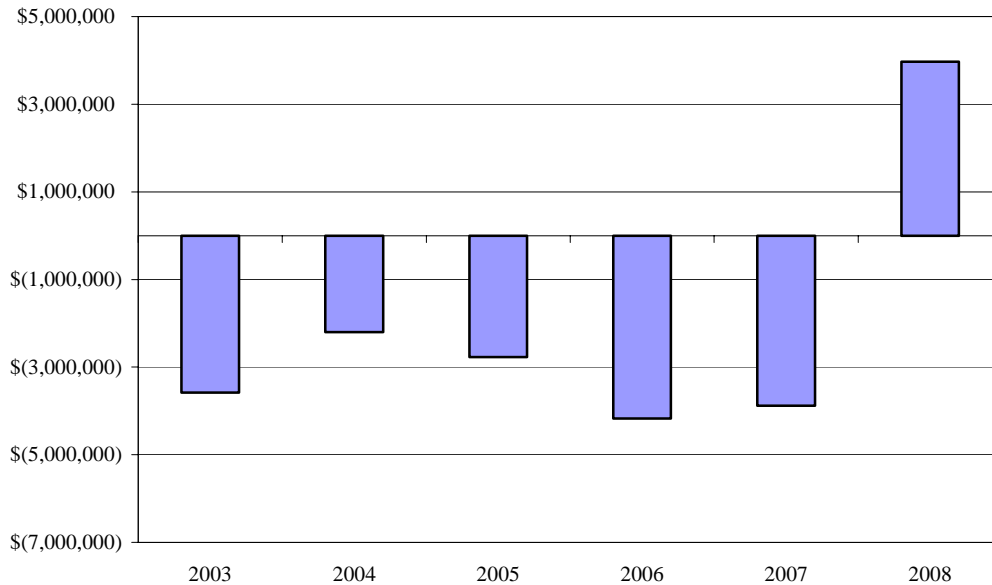
The effect of removing the operational supplements shows the structural imbalance of City taxes, fees and other revenues and the expenditures required for City operations. Does the existing structural imbalance of revenue and expenditures mean that the City of Lancaster is on the brink of declaring Act 47? Even if property tax revenues remain constant through 2012 and only slight increases in other revenue streams are projected, contracted labor costs will still escalate at a greater pace than the increase in revenues. At a conservatively predicted average annual expenditure increase of a million dollars a year, the City’s unreserved fund balance is exhausted by the end of 2008; by the end of 2012 there could be a general fund deficit of \$14.5 million. (See Graphs 10 and 11.)

The City’s seven strategic plan priorities may survive in the strategic plan but the fiscal burden for attaining them cannot be totally borne by the residents of Lancaster City.

Graph 10
 City of Lancaster
Revenue and Expenditures without Supplemental Operational Revenue
 2003 through 2007; 2008 Budget
 [Excluding Non-operational Debt Sources and Uses]



Graph 11 City of Lancaster
Deficit without Operational Supplements
 2003 through 2007; 2008 Budget



CHAPTER 5

CITY OF BETHLEHEM

Bethlehem City has a population of about 72,531 persons (2007 Census estimate) and is the seventh largest city in Pennsylvania. Its population peaked in 1960 at 75,408 persons; in 1970 it decreased to 72,686; in 1980 to 70,419; but increased to 71,329 in 2000. The City has a multiracial population: in the 2000 Census people identifying themselves as whites made up 74.9 percent of the population (87.6 percent in 1990); African American totaled 3.6 percent (2.9 percent in 1990), and those identifying themselves as Hispanic of any race, were at 18.2 percent (13.0 percent in 1990).

City Government

Bethlehem City is governed under an optional plan (strong mayor with council) form of government. Under the Optional Charter Law, the mayor-council form has a seven member council, elected at-large for overlapping four-year terms with an elected treasurer and controller. The mayor is the chief executive of the city and enforces the ordinances of council as well as supervising the work of all city departments and prepares and submits the annual city budget to council.

The Revenue Experience of Bethlehem City

Since 1917, the City of Bethlehem has been divided between the counties of Lehigh and Northampton. On an assessed valuation basis, one-third of the City is in Lehigh County and two-thirds is in Northampton County. The City is not the county-seat for either county. The City borders the Lehigh County seat of Allentown City and is about eight miles from the Northampton County seat of Easton City. While this county split can make regional initiatives and coordination of services more time consuming, there is generally a good working relationship among the three units of government. Both counties conducted property reassessments in 1991, and Northampton County updated assessments in 1995 and 2005. Nonprofits comprise over 19 percent of the City's total assessed valuation.

Home to the Bethlehem Steel Corporation from 1857 to 2003, Bethlehem City was the second-largest steel producer in the United States after Pittsburgh. When the U.S. steel industry

declined and economic problems led to Bethlehem Steel’s bankruptcy in 2001, the company was dissolved and its assets sold. The reduction in scope and the eventual closing of Bethlehem Steel’s facility had a tremendous fiscal impact on the City and the entire Lehigh Valley beyond the loss of jobs. The largest taxable parcel for the corporation was in Bethlehem City; with the company’s bankruptcy, the City’s tax base (both property tax and earned income tax) suffered a major decline over a short period of time. In 2007 the Bethlehem property was sold to Sands Bethworks and the casino (site improvements will be paid from Tax Incremental Financing) is expected to be in operation in 2009. The City will share in the distribution of gaming tax revenue under the Commonwealth’s gaming act. The success of the casino is crucial to the future financial stability of the City of Bethlehem.

The City of Bethlehem has been aggressive in combating the deterioration of its assessable tax base due to the Bethlehem Steel bankruptcy. During the period 2003 to 2007 the City has increased property tax rates by 22.6 percent. While the assessment base rose by just 3.8 percent. The total collection of real estate taxes also improved during the period resulting in an overall increase in real estate revenue of 29.7 percent. (See Table 1.)

Table 1
 CITY OF BETHLEHEM
Real Estate Taxes, Assessed Values, Millage Rates
 2003 - 2007 Actual, 2008 Budget

	<u>Assessment</u>	<u>Millage</u>	<u>Tax Collected</u>	<u>Change</u>					
				<u>Assessed Value</u>		<u>Tax Rate</u>		<u>Taxes Collected</u>	
				<u>\$</u>	<u>%</u>	<u>Mills</u>	<u>%</u>	<u>\$</u>	<u>%</u>
2003	\$1,310,333,000	11.50	\$15,030,431	-	-	-	-	-	-
2004	1,312,358,650	11.75	15,315,668	2,025,650	0.2	0.25	2.17	285,237	1.9
2005	1,322,904,850	12.50	16,820,603	10,546,200	0.8	0.75	6.38	1,504,935	9.8
2006	1,341,312,150	13.96	18,842,927	18,407,300	1.4	1.46	11.68	2,022,324	12.2
2007	1,359,962,300	14.10	19,500,000	18,650,150	1.4	0.14	1.00	657,073	3.5
2008 Budget	1,361,857,550	14.10	20,283,600	1,895,250	0.1	-	-	783,600	4.1
Change 2003-2007									
\$	\$49,629,300	2.60	\$4,469,569	-	-	-	-	-	-
%	3.8%	22.6%	29.7%	-	-	-	-	-	-

A comparison of market values to the recent assessment history of the City shows a lag in the market to assessed valuations for the City. For the period 2003 to 2007, market values have risen by 26.9 percent in the City, while assessed valuations have risen by 3.8 percent.

Northampton County has conducted countywide reassessments in 1991, 1995, and 2005 and applies a predetermined ratio of 50 percent of assessed values to market values. (See Table 2.)

Table 2
CITY OF BETHLEHEM
Market to Assessed Valuations
2003 - 2007

<u>Year</u>	<u>Market Value</u>	<u>Assessed Values Ratio to Market Values</u>
2003	\$2,221,788,800	59.0
2004	2,407,360,700	54.5
2005	2,465,680,700	53.4
2006	2,774,175,100	40.7
2007	2,820,241,700	40.6
Change		
2003-2007		
\$	\$598,452,900	
%		26.9%

SOURCE: State Tax Equalization Board.

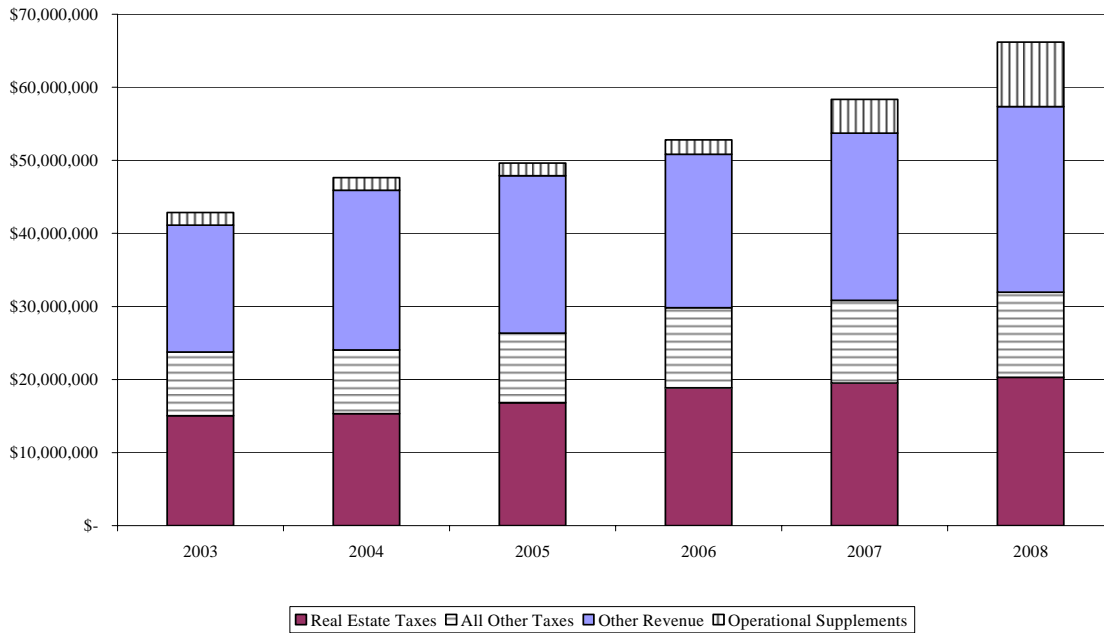
The second largest tax source for the City is the Earned Income Tax (EIT). Based upon City reports, this tax has decreased by 4.4 percent since 2003. The EIT levy experience can be used as a general measure of the earnings of City residents. By law the EIT is levied upon earned income and profits of City residents regardless of their location of employment. The decrease in this revenue source is a challenge to the City as it may indicate growth in a population that does not pay the tax (retired persons or unemployed persons) or that the wages of City residents do not rise significantly from year to year to offset other changes in the population wage base. (See Table 3.)

Table 3
 CITY OF BETHLEHEM
Earned Income Tax
 2003 to 2008 Budget

Year	Total EIT Taxes	Change	
		\$	%
2003	\$ 6,483,983	-	-
2004	6,146,676	-337,307	-5.2
2005	4,949,706	-1,196,970	-19.5
2006	5,807,174	857,468	17.3
2007 Est.	6,200,000	392,826	6.8
2008 Budget	6,600,000	400,000	6.5
Change	\$	-283,983	
2003-2007	%	-4.4%	

In addition to the City’s increased real estate tax rates during the period, the City utilized a “new” revenue source (Local Services Tax—LST) that generated \$1.6 million additional revenue the first year (2005) of levy. By 2007 the LST was yielding slightly more than a third of the total amount received under the EIT. It is important to note that amendments passed in 2007 to the LST legislation caused a 25 percent decline in revenues from this source in the first six months of 2008. (See Graph 1.)

Graph 1 City of Bethlehem
Revenue Components
2003 through 2007; 2008 Budget
[Excluding Non-operational debt]



Further increases in the City’s Real Estate millage rate may become counter productive. Based upon Department of Community and Economic Development statewide data for 2005, Bethlehem City property taxpayers paid a per capita property tax of \$229 compared to \$147 average per capita in the county’s other municipalities. On the earned income tax revenue side, City residents pay a lower per capita amount of their income compared to most other county municipalities. As a result, the per capita earned income tax paid in 2005 by City residents was \$69 compared to the county per capita of \$120. City residents paid EIT at a rate of slightly more than one-half of the per capita tax paid by non-city residents in the remainder of Northampton County.

In 2008, 48.2 percent of the City’s \$64.0 million budgeted General Fund revenues will come from real estate, Act 511, and all other taxes. As the size of the City’s total budget increased by over \$23.0 million from \$42.9 million in 2003 to \$66.2 million in 2008, total taxes increased by \$8.2 million. This increase in the budget exceeded the ability of the city’s taxable base (real estate, earned income, and other business and personal taxes) to provide the additional revenue even with property tax increases of more than 22.0 percent. Consequently, other revenue grew by more than \$15 million since 2003 to provide the needed revenue (See Table 4.)

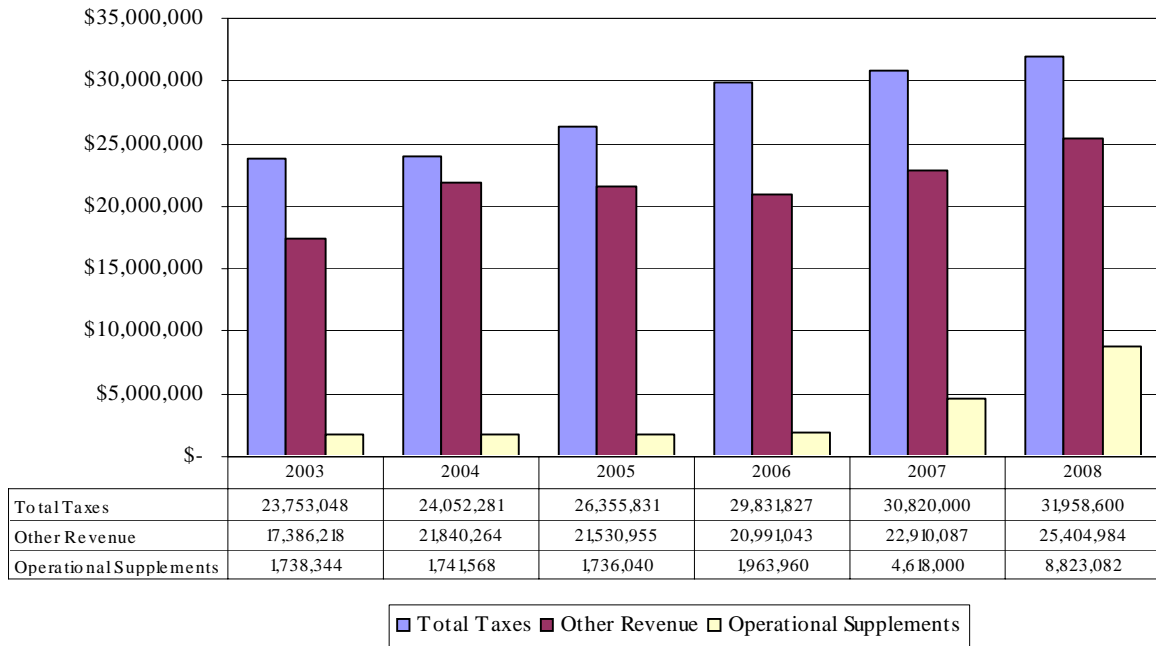
Table 4
CITY OF BETHLEHEM
Dollar and Proportionate Distribution of Revenue From All Sources
2003 to 2008

	<u>2003</u> <u>Actual</u>	<u>2004</u> <u>Actual</u>	<u>2005</u> <u>Actual</u>	<u>2006</u> <u>Actual</u>	<u>2007</u> <u>Actual</u>	<u>2008</u> <u>Budget</u>
Real Estate Taxes	35.1	32.2	33.9	35.7	33.4	30.6
All Other Taxes	20.3	18.3	19.2	20.8	19.4	17.6
Payment in Lieu of Taxes	-	-	-	-	-	-
Other Revenue	40.5	45.9	43.4	39.8	39.3	38.4
Operational Supplements	4.1	3.7	3.5	3.7	7.9	13.3
Non Operational Debt Proceeds	-	-	-	-	-	-
Total Revenue	100.0	100.0	100.0	100.0	100.0	100.0
Real Estate Taxes	\$15,030,431	\$15,315,668	\$16,820,603	\$18,842,927	\$19,500,000	\$20,283,600
All Other Taxes	8,722,617	8,736,613	9,535,228	10,988,900	11,320,000	11,675,000
Payment in Lieu of Taxes	-	-	-	-	-	-
Other Revenue	17,386,218	21,840,264	21,530,955	20,991,043	22,910,087	25,404,984
Operational Supplements	1,738,344	1,741,568	1,736,040	1,963,960	4,618,000	8,823,082
Non Operational Debt Proceeds	-	-	-	-	-	-
Total Revenue	\$42,877,610	\$47,634,113	\$49,622,826	\$52,786,830	\$58,348,087	\$66,186,667
	Change 2003-2008					
	\$	%				
Real Estate Taxes	5,253,169	35.0				
All Other Taxes	2,952,383	33.8				
Total Taxes	8,205,552	34.5				
Payment in Lieu of Taxes	-	-				
Other Revenue	8,018,766	46.1				
Operational Supplements	7,084,739	407.6				
Non Operational Debt Proceeds	-	-				
Other Revenue and Supplements	15,103,505	79.0				
Total Revenue and All Sources	23,309,057	54.4				

Based upon a 2009 casino opening, gaming revenues from 3,000 slot machines should generate \$1.3 million for Bethlehem in 2009 with annual revenue of \$9.1 million projected for 2010. Overall the municipalities of Bethlehem, Allentown, Northampton County and Lehigh County will share a projected \$7.8 million in 2009 and \$19.3 million in 2010. The anticipated revenue from gaming is being used to offset employee healthcare insurance cost increases in the City for 2008 and 2009.

During the review period, operational supplements have been used to meet the gap in needed revenue from the City’s tax base and other revenue sources. These supplemental revenues increased from \$1.7 million in 2003 to \$8.8 million in 2008. (See Graph 2.)

Graph 2
 CITY OF BETHLEHEM
 Taxes Compared to Other Revenue and Operational Supplements
 2003 through 2007; 2008 Budget
 [Excludes non-operational Debt Proceeds]



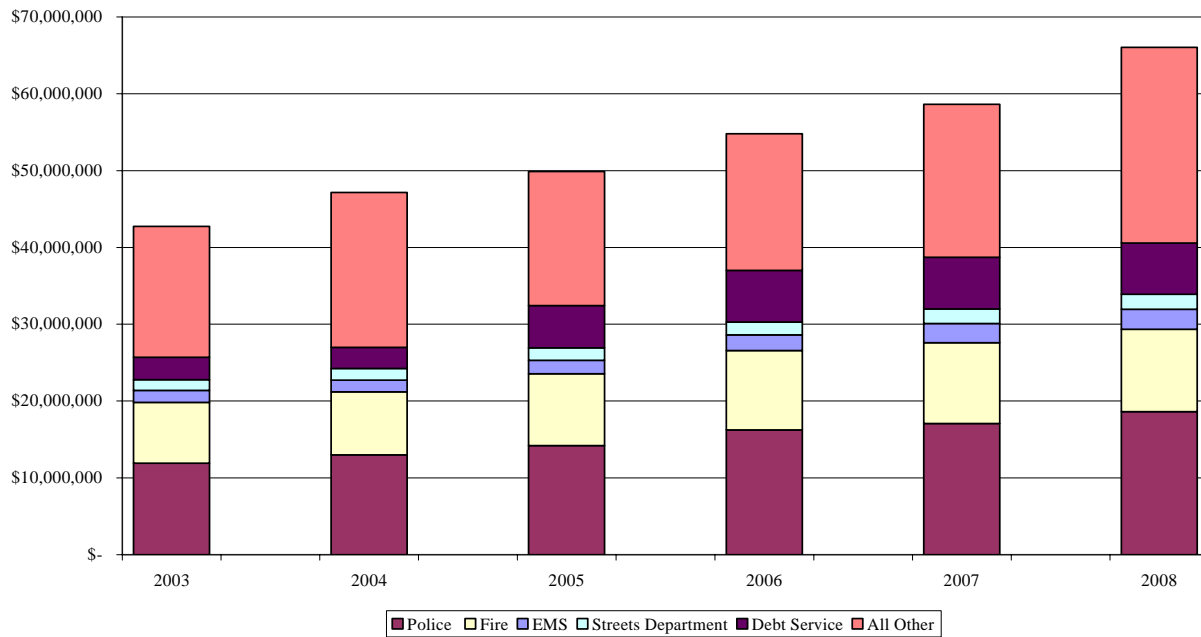
The Expenditure Experience of Bethlehem City

From 2002 to the present, Bethlehem’s general fund spending increased by \$23.3 million (54.5 percent), from \$42.7 million to \$66.0 million. In 2003, 53.3 percent of the City’s expenditures were for Police, Fire, EMS, and Streets. Debt Service was under seven percent and “All Other” category was 39.9 percent. In 2007, that distribution shifted to 54.5 percent for Police, Fire, EMS, and Streets, 11.5 percent for Debt Service and 34.0 percent for “All Other”. For 2008, the City anticipated the mix would further shift to 51.3 percent for Police, Fire, EMS, and Streets, 10.1 for Debt Service, and 38.6 for “All Other.” (See Table 5 and Graph 3.)

Table 5
CITY OF BETHLEHEM
Actual and Budgeted Expenditures
2003 to 2008

	<u>Actual 2003</u>		<u>Actual 2004</u>		<u>Actual 2005</u>		<u>Actual 2006</u>		<u>Actual 2007</u>		<u>Actual 2008</u>		<u>Change 2003 to 2008</u>	
	<u>\$</u>	<u>% of Total</u>	<u>\$</u>	<u>% of Total</u>	<u>\$</u>	<u>% of Total</u>	<u>\$</u>	<u>% of Total</u>	<u>\$</u>	<u>% of Total</u>	<u>\$</u>	<u>% of Total</u>	<u>\$</u>	<u>%</u>
	Police	11,916,897	27.8	12,981,384	27.5	14,196,498	28.5	16,238,217	29.5	17,061,244	29.1	18,611,623	28.2	6,694,726
Fire	7,891,603	18.5	8,211,285	17.5	9,359,336	18.8	10,329,473	18.9	10,513,826	17.9	10,731,934	16.2	2,840,331	36.0
EMS	1,587,857	3.7	1,532,364	3.2	1,755,407	3.5	2,036,393	3.7	2,523,373	4.3	2,607,709	3.9	1,019,045	64.2
Streets Dept.	1,390,319	3.3	1,522,339	3.2	1,606,266	3.2	1,673,753	3.1	1,880,808	3.2	1,962,655	3.0	572,336	41.2
Debt Service	2,910,922	6.8	2,741,227	5.8	5,489,634	11.0	6,715,303	12.3	6,716,559	11.5	6,667,003	10.1	3,756,081	129.0
All Other	<u>17,047,753</u>	<u>39.9</u>	<u>20,162,168</u>	<u>42.8</u>	<u>17,474,561</u>	<u>35.0</u>	<u>17,789,385</u>	<u>32.5</u>	<u>19,940,650</u>	<u>34.0</u>	<u>25,472,742</u>	<u>38.6</u>	<u>8,424,990</u>	<u>49.4</u>
Total Expenditures	42,745,351	100.0	\$ 47,150,767	100.0	49,881,702	100.0	54,782,524	100.0	58,636,460	100.0	66,053,667	100.0	23,308,316	54.5

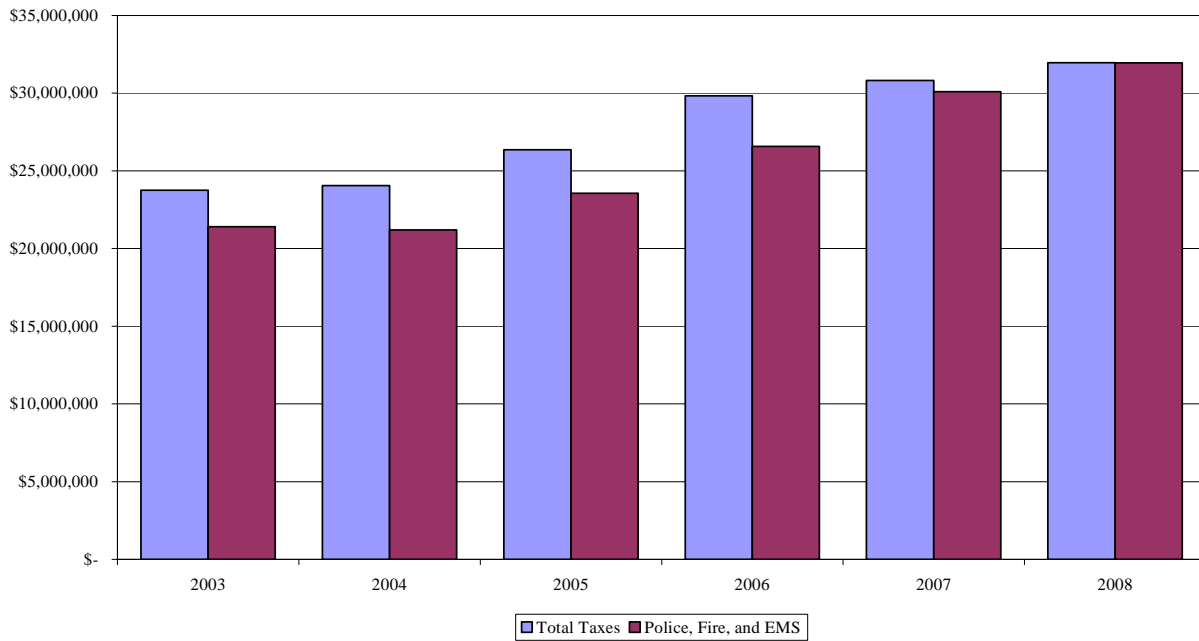
Graph 3
 CITY OF BETHLEHEM
 Expenditure Components
 2003 through 2007; 2008 Budget
 [Excluding Non-operational Debt Uses]



The City’s stated goal of providing services to ensure that it is “Clean and Safe” is perhaps Mayor John Callahan’s most often used phrase in describing the administration’s goals. Public Safety (Police, Fire, and EMS) expenditures have risen during the review period by 49.3 percent while Total Taxes have increased by 34.6 percent. The current cost of public safety is only slightly less than the amount of total taxes available to Bethlehem. However, in the future, the continued increase of revenues may not be sufficient to cover the public safety costs without further tax increases. (See Graph 4.)

To maintain a “Clean and Safe” City environment, ten police officers have been added to the force since 2004, three of them through the PA COPS funding initiative. During the prior 20 year period, (1984-2004) the police department had increased by 12 officers. The current 154 person police force has seen a reduction in violent crime of eight percent since 2004 with total crime down 5.7 percent since 2006. The City’s 2009 and 2010 budgets will include plans to hire an additional four officers each year. The cost for the Police Department rose by 44.3 percent from actual 2003 costs to the 2008 budget estimates.

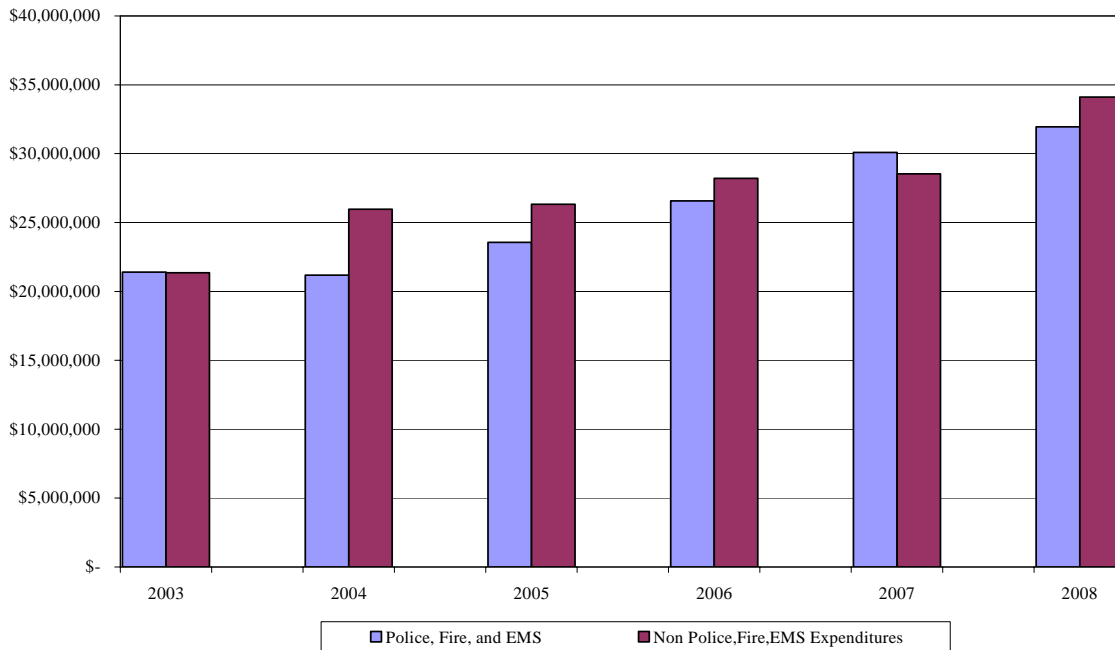
Graph 4
 CITY OF BETHLEHEM
 Police, Fire and EMS Expenditures Compared to Total Taxes
 2003 through 2007; 2008 Budget



Bethlehem’s fire department has 114 officers with a minimum manning requirement that increases shift requirements by two firefighters in 2009. The expenditures for the Fire Service rose by 36.0 percent for the review period. Firefighters are not required to provide Basic or Advanced Life Support for citizens. The City has a separate paramedic corps of 24 employees that provides this service and reports to the Fire Department.

Unlike other cities reviewed, Bethlehem’s Public Safety expenditures did not exceed the total of “All Other Expenditures” in 2004, 2005, 2006, and 2008. (See Graph 5.)

Graph 5
 CITY OF BETHLEHEM
Police, Fire, and EMS Compared to All Other Expenditures
 2003 through 2007; 2008 Budget
 [excluding non operational debt uses]



Expenditures for other public safety services include the City’s 30-year long provision of its own 911 center due to the geographic split between two counties.

Streets Department expenditures have grown by more than \$572,000 or 41.2 percent during the review period.

As a way to manage the increasing cost of medical insurance for City employees, the insurance provider and the City agreed to defer increases in medical insurance beyond a specified base expense until expected gaming revenues are received. All employees pay premium co-pays of \$35 per month regardless of the type of employee coverage.

Debt Service has increased during the review period by more than \$3.8 million or by 129.0 percent. In 2003, Debt Service expenditures were \$2.9 million, in 2008 the City has budgeted \$6.7 million for Debt Service. Note that two percent of the City’s total debt is payment on a 1997 federal civil rights judgment against Bethlehem as a result of a wrongful death suit. The City was underinsured for the over \$7 million judgment and is paying \$880,000 a year for 12 years.

Operational Supplements

The City has used operational supplements in each budget year during the review period to mitigate the growing gap between expenditures and traditional revenues and has used the proceeds to balance the budget, prevent deficits, and continue to provide services to residents. As a percentage of all other revenues realized by the City for the review period, these operational supplements range from 3.6 percent in 2005 to 13.3 percent in budget year 2008. The inclusion of these Operational Supplements from the revenue side and the resultant surplus or deficit of revenues over expenditures is shown in Graph 6. The source of funds for the Operational Supplements varies from year to year; for example the Supplements include funds from Operations from Water and Sewer, Bethlehem Parking Authority, Urban Development Action and Community Development Block grants, Sewer Tap-in fees, Suburban Stakeholders Agreement, and from Deferred Expenditures. (See Table 6 and Graph 7.)

Graph 6
 CITY OF BETHLEHEM
 Surplus (Deficit) Including Operational Supplements
 2003 through 2007; 2008 Budget

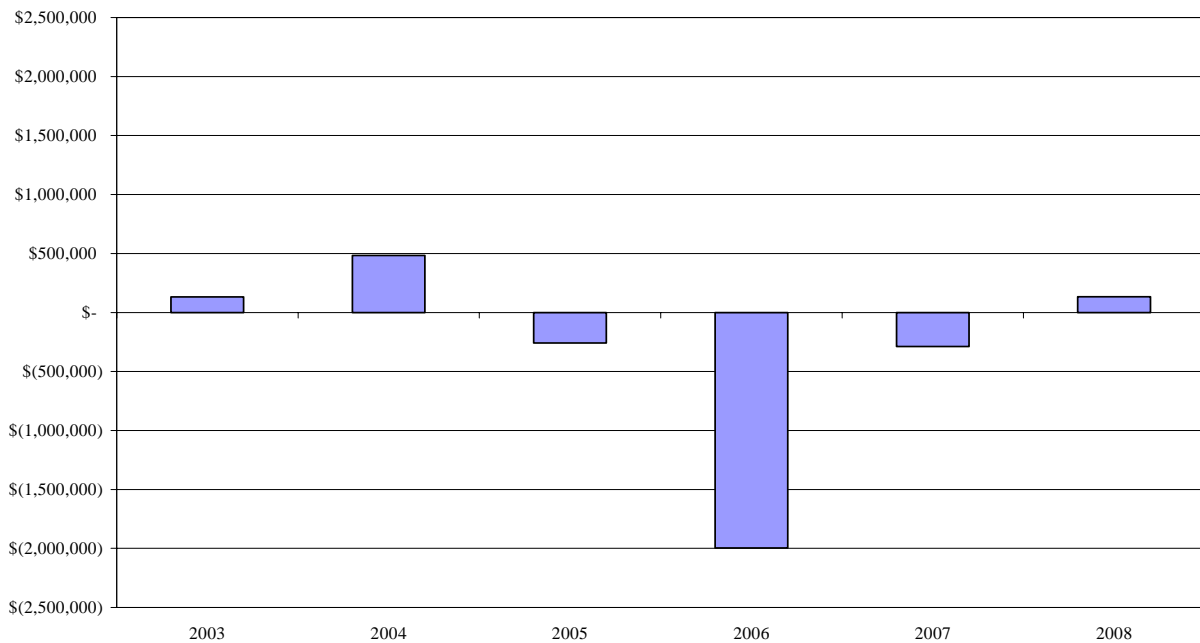
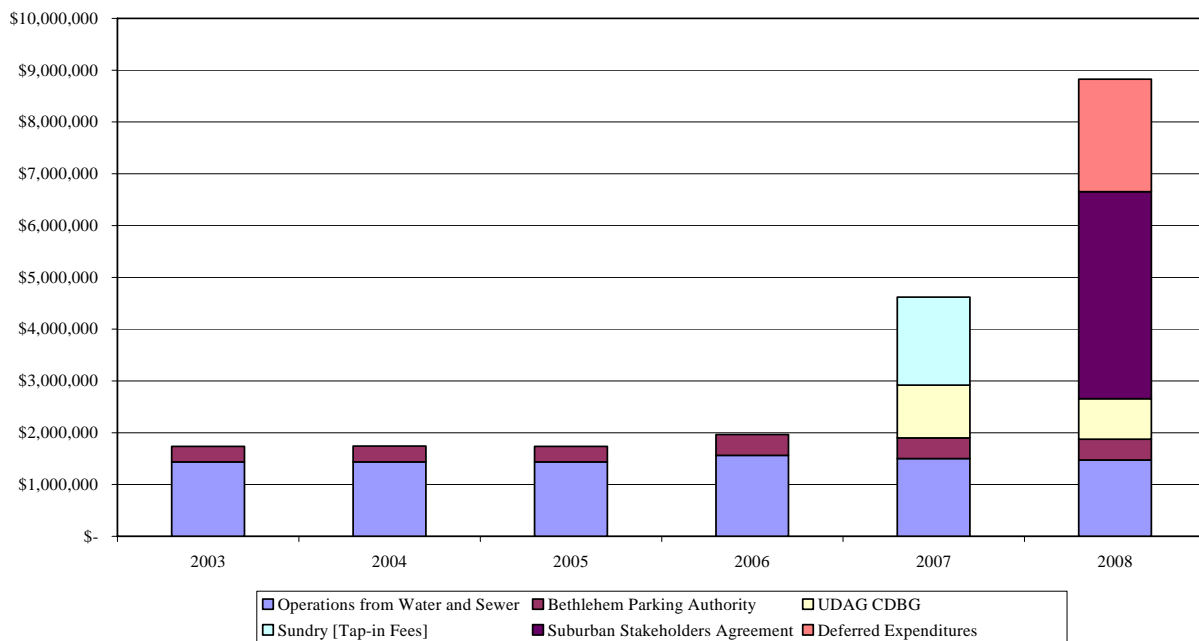


Table 6
CITY OF BETHLEHEM
Operational Supplements
2003 through 2007; 2008 Budget

	2003 <u>Actual</u>	2004 <u>Actual</u>	2005 <u>Actual</u>	2006 <u>Actual</u>	2007 <u>Actual</u>	2008 <u>Budget</u>
Operations from Water and Sewer	\$1,436,040	\$1,436,040	\$1,436,040	\$1,563,960	\$1,500,000	\$1,474,416
Bethlehem Parking Authority	302,304	305,528	300,000	400,000	400,000	400,000
UDAG CDBG	-	-	-	-	1,018,000	782,000
Sundry [tapping Fees]	-	-	-	-	1,700,000	-
Suburban Stakeholders Agreement	-	-	-	-	-	4,000,000
Deferred Expenditures	-	-	-	-	-	<u>2,166,667</u>
Total Operational Supplements	\$1,738,344	\$1,741,568	\$1,736,040	\$1,963,960	\$4,618,000	\$8,823,082
Percent of All Other Revenues	4.2%	3.8%	3.6%	3.9%	8.6%	15.4%

During the review period, there was an increased reliance on the use of funds from the sewer fund and a decreased reliance on the water fund. Together, the funds provided up to \$1.5 million in supplements; the 2008 budget estimated use from these funds of \$1.47 million. The City sewer operations are attempting to provide uniformity of service within the serviced area, therefore, Bethlehem City is updating the language of the sewer provision agreements (some 30 to 40 years old) with the nine serviced townships. The City has a municipal asset in its

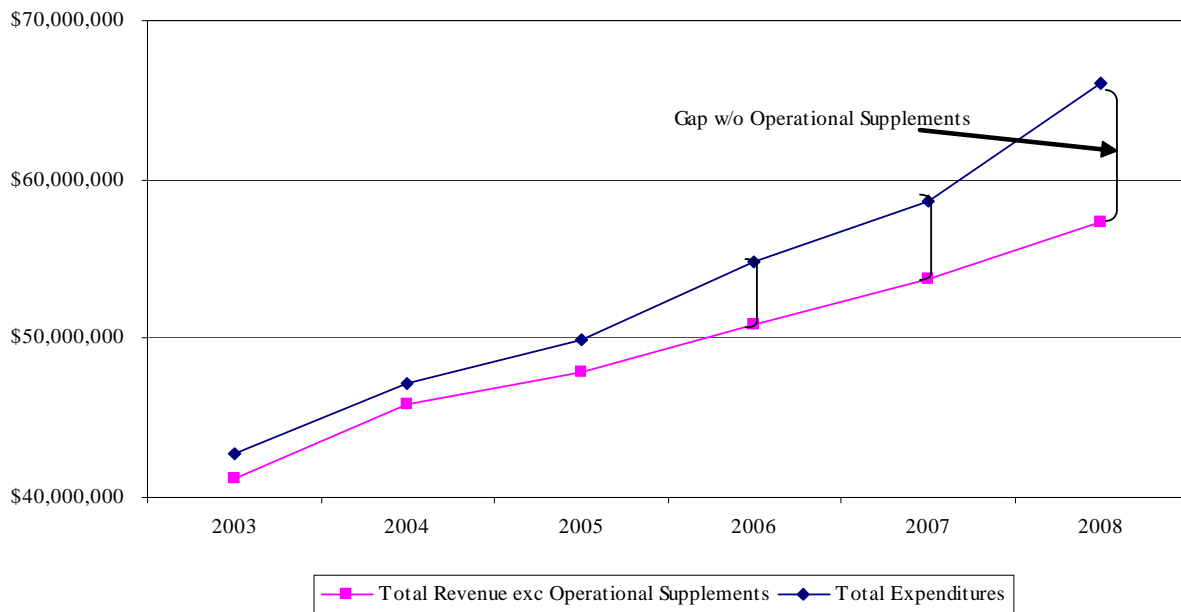
Graph 7
CITY OF BETHLEHEM
Operational Supplements
2003 through 2007; 2008 Budget



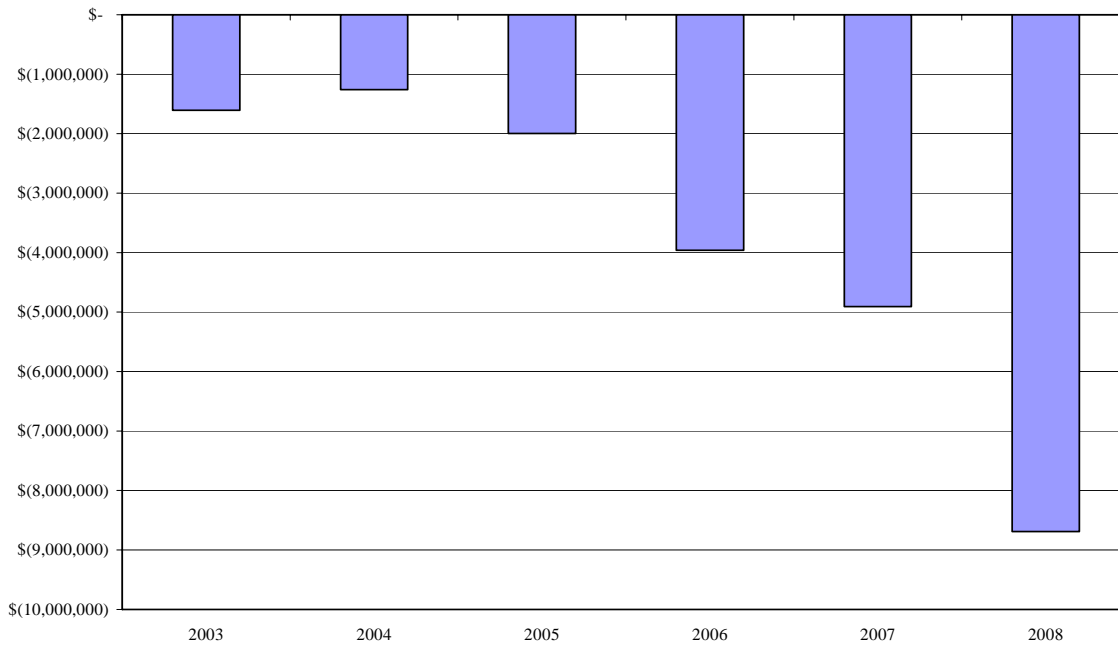
wastewater treatment plant and can provide sewerage capacity for a reasonable cost. The City anticipates significant revenue from its sewer capacity over the next three and one-half years; however the City will have to participate in capital improvements to the system to maintain this capacity. These capital requirements may reduce the amount of supplemental revenue that is available for the City to utilize in future budgets.

The role of operational supplements in balancing the City’s budget has grown during the review period, particularly since 2005. If the operational supplements are excluded from the available revenue that the City could utilize, and expenditure levels are maintained at needed levels, the result would be that the City exceeded its expenditures over its revenue every year since 2003. The amount of excess varied, but since 2005 the supplements have become increasingly necessary even with the City’s increases in the real estate millage during the same period. (See Graphs 8 and 9.)

Graph 8 CITY OF BETHLEHEM
Revenue without Operational Supplements vs. Expenditures
 2003 through 2007; 2008 Budget
 [Excluding Non-operational Debt Sources and Uses]



Graph 9
 CITY OF BETHLEHEM
Deficit without Operational Supplements
 2003 through 2007; 2008 Budget



Several popular magazines have written of Bethlehem as a desirable city, as one of the best places to live and raise a family and as one of the 1,000 places to see before you die. FORTUNE magazine in July 2008 ranked Bethlehem as the 58th best city for small business. It would seem that the grim past economic condition defined by Bethlehem Steel’s bankruptcy has given way to a reframed municipal identity. **If anticipated casino local share revenue remains available for the City to utilize then Bethlehem may be financially stable; if for whatever reason the local share does not materialize, increasing expenditures and the need to balance revenue increases against will be necessary. In the future, without the anticipated casino revenues, Bethlehem will likely be in the same fiscally challenging situation as the other case study municipalities.**

CHAPTER 6

CITY OF YORK

The City of York has a population of 40,226 persons (2007 Census estimate) and is the 13th largest city in Pennsylvania. Almost due west of Philadelphia, southeast of Harrisburg, and southwest of Lancaster, the City is the county seat of York County. In 1970, the population totaled 50,335 persons, declining to 40,862 in 2000. The City has a diverse racial makeup: in the 2000 Census, people identifying themselves as white made up 60 percent of the population, African American were 25 percent, and Hispanic of any race, 17 percent or 7,026 persons. In 1990, 72.5 percent of the people identified themselves as white, 21.3 percent as African-American and the Hispanic population of all races was 3,244 persons or 7.7 percent. For the period of 2005-2007, the U.S. Census Bureau reported that York had a significantly high poverty level with an estimated 33 percent of its population defined to be at or below the poverty level.

City Government

The City of York is a third class city under an optional plan (Mayor/Council) form of government. The Mayor, as chief executive officer, has the power to appoint all department heads including the City's Business Administrator. City Council is made up of five members elected at large. There is also an elected Treasurer and elected Controller. The City's workforce totaled 413 full time employees in 2003, a reduction from 463 in 1999. By October 2008, the City's workforce had been further reduced to 356 full-time employees.

Mayor John Brenner was first elected in November of 2001 and was re-elected in 2005. He is, as chief executive officer, responsible for the development of the City's budget and maintenance of finances principally through the Business Administrator. The Mayor presents an annual budget message and also gives a yearly address on the State of the City.

In 2005-2006 the City of York participated in the Governor's Center for Local Government Services' Early Intervention Program (EIP). The purpose of the EIP program is to analyze a municipality's fiscal and management situation and prepare a five year financial plan to address financial and budget challenges. The EIP found that there were significant financial issues facing the City and offered a variety of recommendations to improve the situation. The focus of the City's financial difficulties centered on a static revenue base versus increasing personnel costs especially in the area of medical insurance and pensions. One of the most urgent

issues facing the City was a court decision which mandated the payment of unfunded pension benefits, based on a dispute in the method of pension calculations. The City’s actuary determined that the unfunded accrued liability related to this decision amounted to a \$26.5 million liability for the City.

The City has instituted a number of the EIP recommendations including the procedure for funding the additional pension obligation, the passage of an amusement and parking tax; raising various fees; development of a comprehensive medical insurance plan through the use of an outside consultant; and attempts to control other labor costs. Police and fire contracts, however, are either currently in arbitration or litigation.

The Revenue Experience of the City of York

The principal revenue sources for municipalities in Pennsylvania are the Real Estate Tax and the Earned Income Tax. The last countywide reassessment for York County occurred in 2006 and increased the City’s real estate tax base by about \$116 million. However, the new assessment base immediately began to decline, dropping by almost \$2 million by 2008 as appeals to the new values were granted. (See Table 1.)

Table 1
CITY OF YORK
Real Estate Taxes, Assessed Values, Millage Rates
2003 - 2007 Actual, 2008 Budget

Year	Assessment	Millage	Taxes Levied	Taxes Collected	Change					
					Assessed Valuation		Tax Rate		Taxes Collected	
					\$	%	Mills	%	\$	%
2003	\$888,323,840	11.39	\$10,118,009	\$ 9,866,892	-	-	-	-	-	-
2004	883,871,428	12.52	11,066,070	10,912,637	-4,452,412	-0.50	1.13	9.92	1,045,744.96	10.60
2005	882,343,293	13.52	11,929,281	11,543,864	-1,528,135	-0.17	1.00	7.99	631,227.81	5.78
2006	998,627,633	13.17	13,151,926	12,974,418	116,284,340	13.18	-0.35	-2.59	1,430,553.47	12.39
2007	997,818,478	13.67	13,640,179	13,484,516	-809,155	-0.08	0.50	3.80	510,097.69	3.93
2008 Budget	996,713,759	14.67	14,621,791	14,231,269	-1,104,719	-0.11	1.00	7.32	746,753.36	5.54
Change										
2003-2007										
\$	\$10,949,638	2.28	\$3,522,170	\$3617,624	-	-	-	-	-	-
%	12.3%	20.0%	34.8%	36.7%	-	-	-	-	-	-

Note: Taxes Collected included General Fund (City Unaudited), Debt Service Fund and Recreation Fund (Audited)

In an effort to offset the tax base decline and meet the need from rising expenditures, the City increased its millage rate from 13.17 mills in 2006 to 14.67 or 2008. York City levies separate millages for general purposes (General Fund), recreation purposes and debt service.

As a result of millage increases, total real estate taxes collected increased from the initial \$9.8 million in 2003 to an estimated \$14.2 million for the 2008 budget. Even with a current reassessment, there is not enough yearly growth in the real estate tax base to meet the City’s fiscal demands. (See Table 2.)

Table 2
 CITY OF YORK
Millage Rates
 2003 - 2007 Actual, 2008 Budget

<u>Year</u>	<u>General Fund</u>	<u>Recreation</u>	<u>Debt Service</u>	<u>Total</u>
2003	8.770	1.000	1.620	11.390
2004	9.115	1.000	2.405	12.520
2005	9.853	1.000	2.667	13.520
2006	9.783	1.000	2.387	13.170
2007	10.343	1.000	2.327	13.670
2008	11.392	1.000	2.278	14.670

The City’s reported market value is less than the assessed value with a ratio over 100 percent; as a result, assessments may tend to decline to the level of the market value over the next few years. Raising real estate millage will likely remain the only means to provide meaningful additional real estate tax dollars. (See Table 3.)

Table 3
 CITY OF YORK
Market to Assessed Valuations
 2003 - 2007

<u>Year</u>	<u>Market Value</u>	<u>Assessed Values Ratio to Market Values</u>
2003	\$732,989,600	121.2
2004	768,884,800	115.2
2005	767,365,700	115.2
2006	810,598,400	123.4
2007	805,653,500	124.2
Change 2003-2007		
\$	\$72,663,900	
%		9.9%

SOURCE: State Tax Equalization Board.

Special Fund Accounting

A brief comment needs to be made regarding the treatment of tax receipts by the City of York. The City levies separate millage rates for general purposes, debt service and recreation; and accounts for these real estate taxes in three separate funds, the General Fund, the Debt Service Fund and the Recreation Fund. To get a proper measure of the City’s total tax situation, PEL combined the revenues of these funds into one combined fund. To keep the measurement balanced, expenditures for all three funds were also totaled into one fund. The data used for this purpose was gathered from the unaudited City General Fund and audits for debt service and recreation funds.

Earned Income Tax

York has an Earned Income Tax (EIT) rate of 0.5 percent. For the review period 2003 through 2008, the City’s EIT collections have averaged \$2.15 million yearly. Based upon the period 2004 through 2008 (excluding the collections reported in 2003 which may have been received and reported in 2002) the EIT increased by \$72,778 or 3.3 percent from 2004 through 2008. (See Table 4.)

Table 4
CITY OF YORK
Earned Income Tax
2003 - 2007 Actual, 2008 Budget

Year	% Rate	Total EIT Taxes	Change	
			\$	%
2003	0.5	1,803,577	-	-
2004	0.5	2,227,222	423,645	23.5
2005	0.5	2,188,099	-39,123	-1.8
2006	0.5	2,241,056	52,957	2.4
2007	0.5	2,133,675	-107,381	-4.8
2008 Budget	0.5	2,300,000	166,325	7.8
Change 2004-2008				
	\$	\$72,778		
	%	3.3%		
Average Yearly Collections 2003-08		\$2,148,938		

Taxes and Other Revenue

Table 5 provides a summary of the General Fund, Debt Service Fund, and Recreation Fund for the City of York for 2003 through 2008. Over the review period, Total Revenue has increased from \$33.6 million in 2003 to \$40.6 million for the 2008 budget estimate, a \$6.9

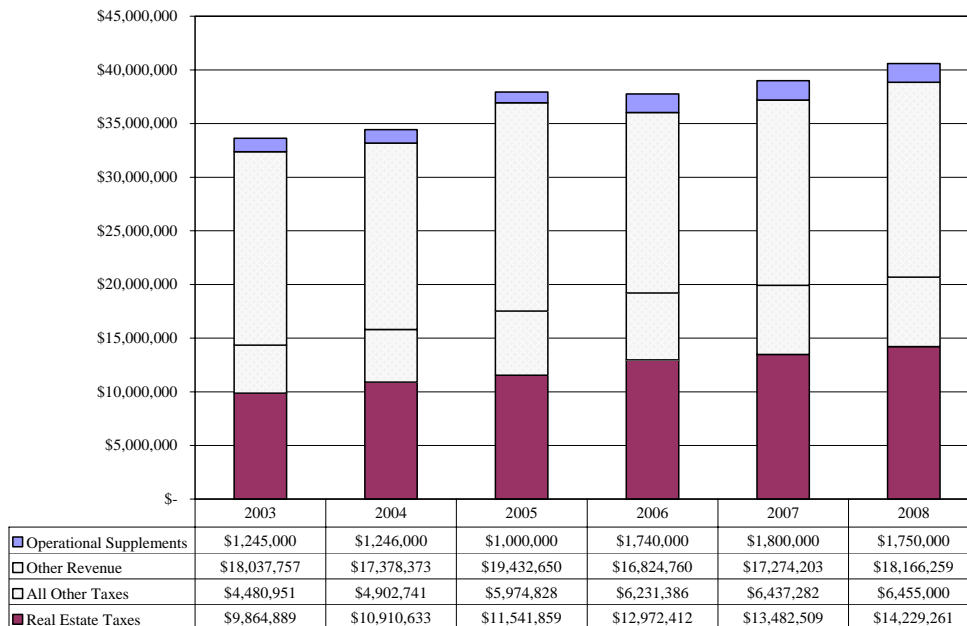
million or 20.7 percent change. Real Estate Taxes grew by \$4.4 million or 44.2 percent over the period.

Table 5
CITY OF YORK
Revenue Components
2003 to 2008

	2003	2004	2005	2006	2007	2008	Change	
	<u>Actual</u>	<u>Actual</u>	<u>Actual</u>	<u>Actual</u>	<u>Actual</u>	<u>Budget</u>	\$	%
Real Estate Taxes	\$9,864,889	\$10,910,633	\$11,541,859	\$12,972,412	\$13,482,509	\$14,229,261	\$4,364,372	44.2
All Other Taxes	4,480,951	4,902,741	5,974,828	6,231,386	6,437,282	6,455,000	1,974,049	44.1
Other Revenue	18,037,757	17,378,373	19,432,650	16,824,760	17,274,203	18,166,259	128,502	0.7
Operational Supplements	<u>1,245,000</u>	<u>1,246,000</u>	<u>1,000,000</u>	<u>1,740,000</u>	<u>1,800,000</u>	<u>1,750,000</u>	<u>505,000</u>	40.6
Total Revenue	\$33,628,596	\$34,437,747	\$37,949,338	\$37,768,557	\$38,993,993	\$40,600,520	\$6,971,924	20.7

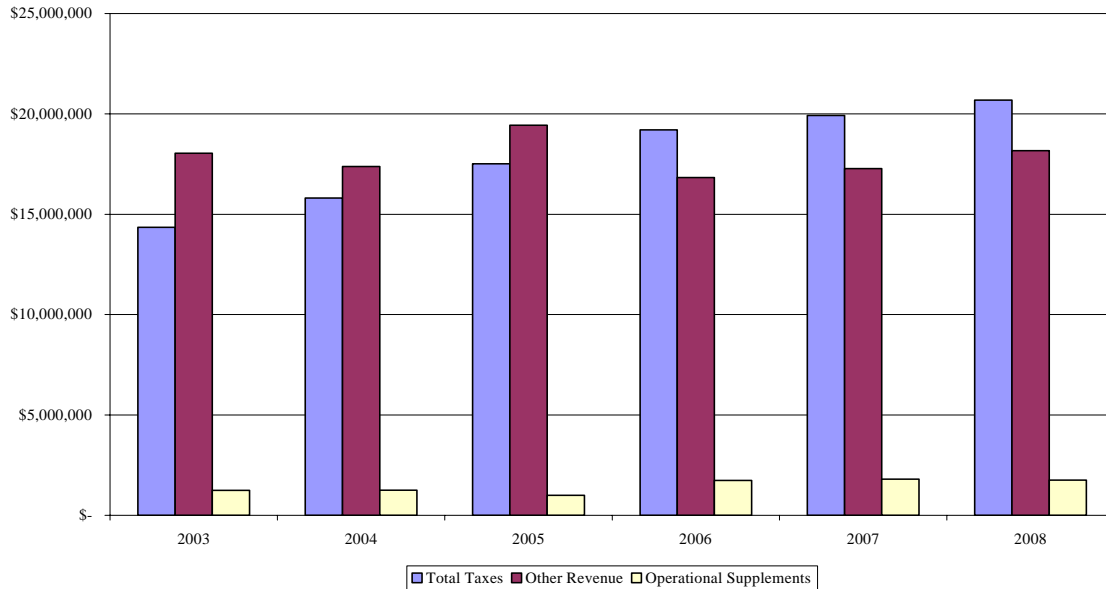
Excluding the countywide reassessment, there has been little growth in the City’s real estate tax base. Revenue growth from real estate resulted from increasing the millage rate. The principal reasons for the growth in all other taxes was the levy of the Local Services Tax (LST) in 2005, and the levying of amusement and parking taxes in 2008, and the use of operational supplements. (See Graph 1.)

Graph 1 CITY OF YORK
Revenue Components
2003 through 2007; 2008 Budget



There has been a steady growth in total taxes over the period 2003 through budget 2008. “Other Revenue” category fluctuates, ranging from \$16.8 million in 2006 to \$19.4 million in 2005. The “Operational Supplement” Category also increased from under \$1.3 million in 2003, 2004, and 2005 to \$1.75 and \$1.8 million for 2007 and 2008, respectively. (See Graph 2.)

Graph 2 City of York
Taxes; Other Revenue; Operational Supplements
2003 through 2007; 2008 Budget



The Expenditure Experience of the City of York

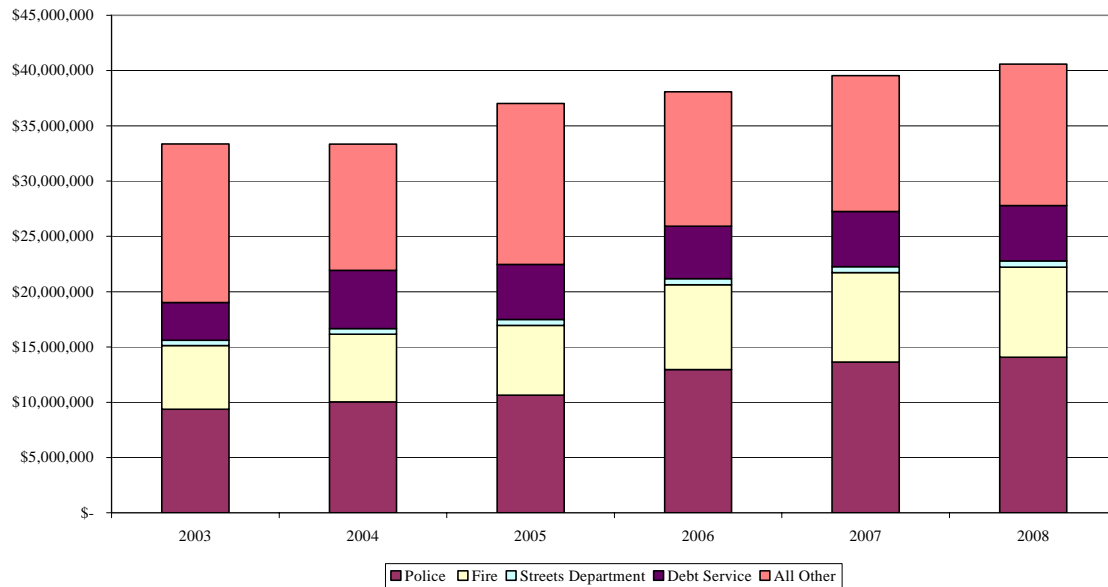
Table 6 provides a summary of expenditures for the City of York from 2003 through the 2008 budget estimate. Expenditure categories include the General Fund, Debt Service Fund, and the Recreation Fund, funds that have tax dollars as part of the revenue source.

Table 6
CITY OF YORK
Expense Components
2003 - 2007 Actual, 2008 Budget

	2003	2004	2005	2006	2007	2008	Change 2003-08	
	Actual	Actual	Actual	Actual	Actual	Budget	\$	%
Police	\$9,370,827	\$10,027,500	\$10,650,439	\$12,954,553	\$13,637,647	\$14,080,471	\$4,709,644	50.3%
Fire	5,757,467	6,131,144	6,297,645	7,671,357	8,088,813	8,150,143	2,392,677	41.6
Streets Department	475,614	503,021	538,548	553,698	538,358	562,489	86,875	18.3
Debt Service	3,419,261	5,260,827	4,995,156	4,749,096	4,998,710	4,997,950	1,578,689	46.2
All Other	14,351,426	11,432,806	14,551,137	12,152,067	12,274,904	12,790,102	-1,561,324	-10.9
Total Expenditures	\$33,374,594	\$33,355,298	\$37,032,924	\$38,080,771	\$39,538,432	\$40,581,155	\$7,206,561	21.6%

Total expenditures have increased from \$33.4 million in 2003 to \$40.6 million for the 2008 budget estimate, a \$7.2 million or 21.6 percent increase. (See Graph 3.)

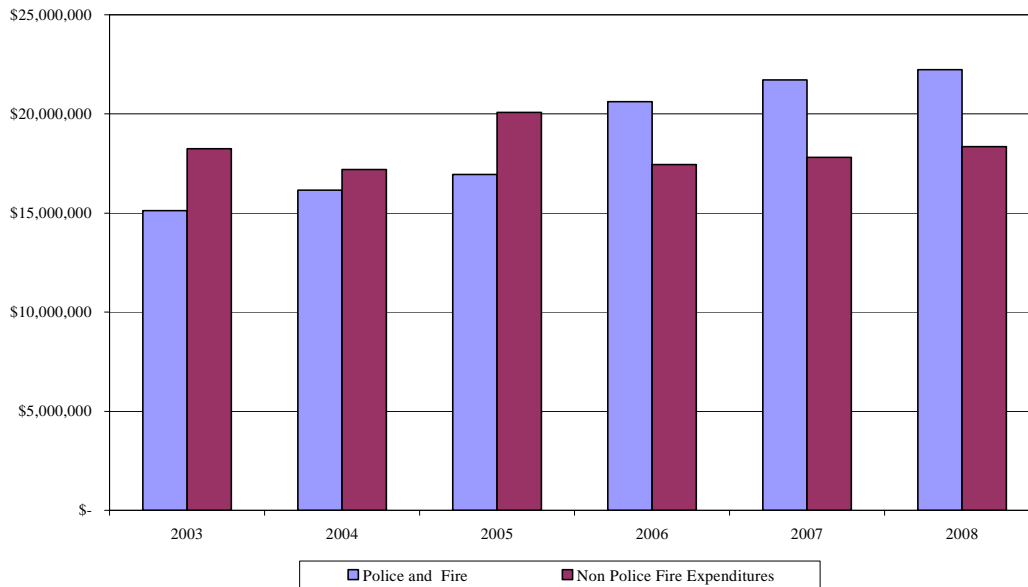
Graph 3 City of York
Expenditure Components
2003 through 2007; 2008 Budget



Over the review period, police expenditures increased by \$4.7 million dollars or 50.3 percent; fire expenditures increased by \$2.4 million or 41.6 percent; and debt service increased by \$1.6 million or 46.2 percent. (Much of this general obligation debt service relates to debt incurred prior to 2003, specifically bond issues of 1995 and note issues of 1998 and 2002.) Finally, “All Other” expenditure category has fluctuated over the period with a high in 2003 at \$14.4 million and a low of \$11.4 million in 2004, averaging \$12.9 million yearly.

Police and fire expenditure changes can also be measured against all other expenditures including debt service. In 2003 police and fire were 82.9 percent of all other expenditures; by 2008 police and fire were 121.1 percent of all other expenditures. (See Graph 4.)

Graph 4 City of York
Police and Fire Compared to All Other Expenditure
2003 through 2007: 2008 Budget



Total Taxes vs. Police and Fire Expenditures

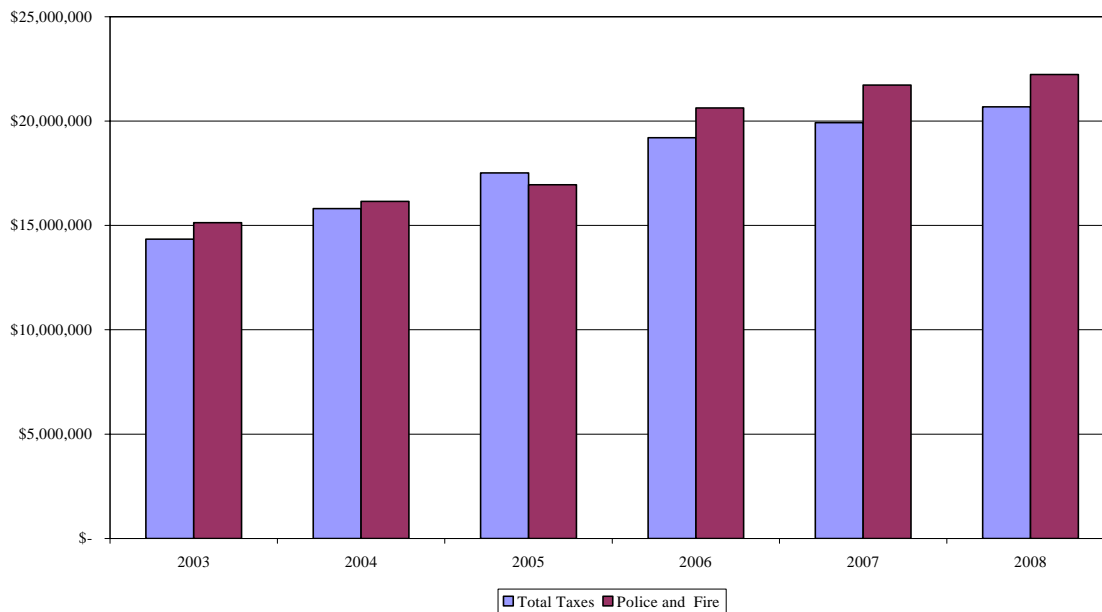
Taxes have historically provided the revenue stream to fund the bulk of local government services and citizens generally believe that their taxes pay for all the government services they require.

Table 7 and Graph 5 depict total taxes compared to police and fire expenditures for 2003 through 2008 budget.

Table 7
CITY OF YORK
Police and Fire Expenditures Compared to Total Taxes
2003 - 2007, 2008 Budget

	2003 <u>Actual</u>	2004 <u>Actual</u>	2005 <u>Actual</u>	2006 <u>Actual</u>	2007 <u>Actual</u>	2008 <u>Budget</u>
Total Taxes	\$14,345,839	\$15,813,373	\$17,516,688	\$19,203,798	\$19,919,790	\$20,684,261
Police and Fire	15,128,293	16,158,644	16,948,084	20,625,910	21,726,460	22,230,614
Difference in Dollars	782,454	345,271	-568,604	1,422,112	1,806,670	1,546,353
As a Percentage of Total Taxes	94.8%	97.9%	103.4%	93.1%	91.7%	93.0%

Graph 5 City of York
Police and Fire Expenditures Compared to Total Taxes
2003 through 2007; 2008 Budget



In every year except 2005, police and fire expenditures were greater than the total taxes collected by the City. The excess of police and fire expenditures over total tax revenues ranged from a low of about \$345,000 in 2004 to a high of \$1.81 million in 2007. In York City, all locally collected tax dollars are insufficient to meet the costs of providing police and fire services.

Part of the City’s police and fire cost structure is related to a court decision requiring the City to increase contributions to police and fire pension trust funds. York City was able to secure special legislation which permitted the additional \$25.6 million unfunded actuarial liability to be amortized over thirty years. The actual funding contributions for all City pensions in presented in Table 8.

Table 8
CITY OF YORK
Pension Funding Requirements
2003 - 2007, 2008 Budget

	2004 <u>Actual</u>	2005 <u>Actual</u>	2006 <u>Actual</u>	2007 <u>Actual</u>	2008 <u>Budget</u>
Officers & Employees	\$ 295,282	\$ 316,290	\$ 291,572	\$ 331,360	\$ 335,270
Police	1,087,478	1,172,257	2,949,964	2,988,309	3,052,400
Fire	<u>509,242</u>	<u>545,584</u>	<u>1,621,527</u>	<u>1,641,164</u>	<u>1,681,387</u>
Total	\$1,892,002	\$2,034,131	\$4,863,063	\$4,960,833	\$5,069,057

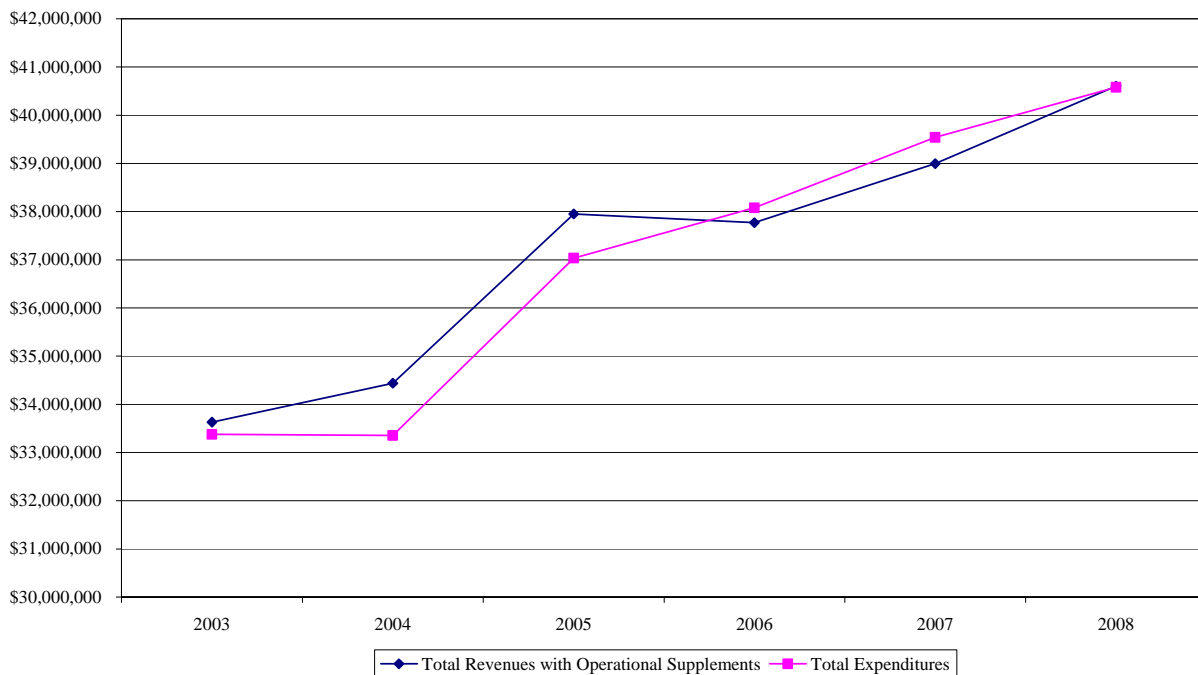
Total Revenues and Expenditures

Table 9 presents Total Revenues and Expenditures for the City of York for the General Fund, Recreation Fund, and Debt Service Fund for 2003 through the 2008 budget. From 2003 through 2005, revenues exceed expenditures. However in 2006 and 2007 expenditures were greater than revenue. For 2008 the budget for revenue and expenditures is just about break even. (See Graphs 6 and 7.)

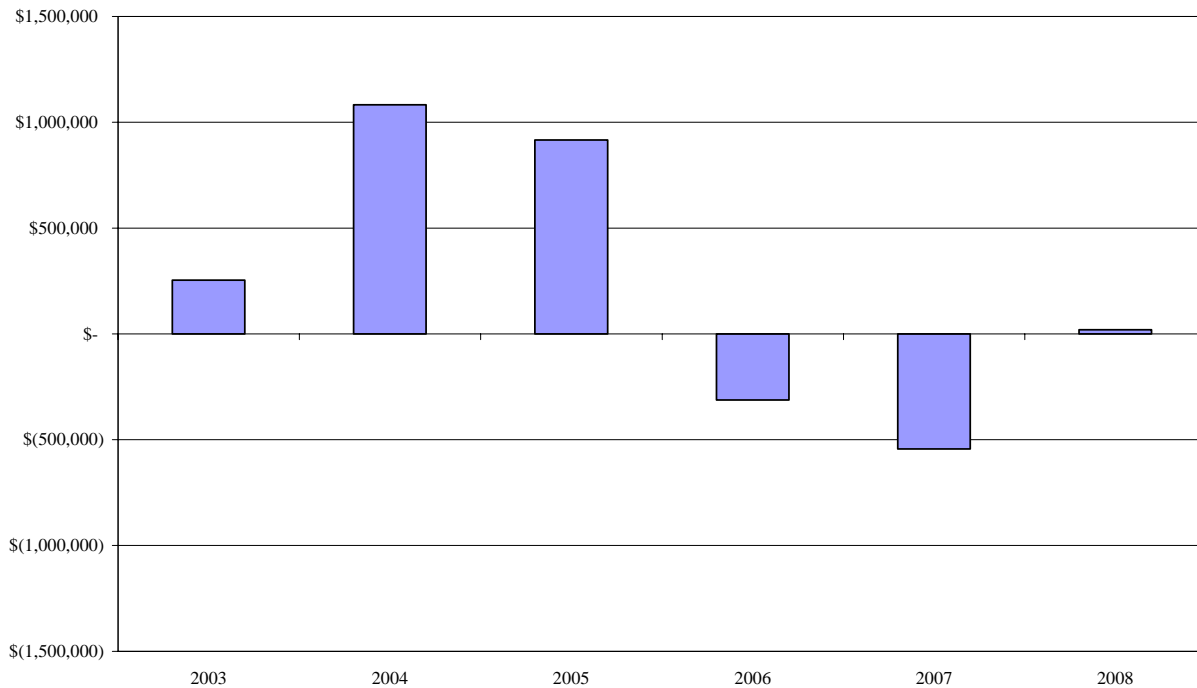
Table 9
CITY OF YORK
Total Revenues with Operational Supplements vs. Total Expenditures
2003 - 2007, 2008 Budget

	2003 <u>Actual</u>	2004 <u>Actual</u>	2005 <u>Actual</u>	2006 <u>Actual</u>	2007 <u>Actual</u>	2008 <u>Budget</u>
Total Revenues with Operational Supplements	33,628,596	34,437,747	37,949,338	37,768,557	38,993,993	40,600,520
Total Expenditures	33,374,594	33,355,298	37,032,924	38,080,771	39,538,432	40,581,155
Surplus (Deficit)	254,002	1,082,449	916,414	(312,214)	(544,439)	19,365

Graph 6 CITY OF YORK
Revenues With Operational Supplements and Expenditures
2003 through 2007; 2008 Budget



Graph 7 CITY OF YORK
 Surplus (Deficit)
 2003 through 2007; 2008 Budget
Includes All Operational Supplement Funds



In 2006 the City began to fund the additional required pension amortization. Also, in 2006 and 2007, the City was faced with a major liability claim of approximately \$2 million and in 2007 borrowed funds to pay off this liability.

The cost escalation facing the City is significantly outpacing the City’s static revenue bases, especially the real estate tax base and residential earned income tax. The Early Intervention Study performed by Public Financial Management (PFM) states:

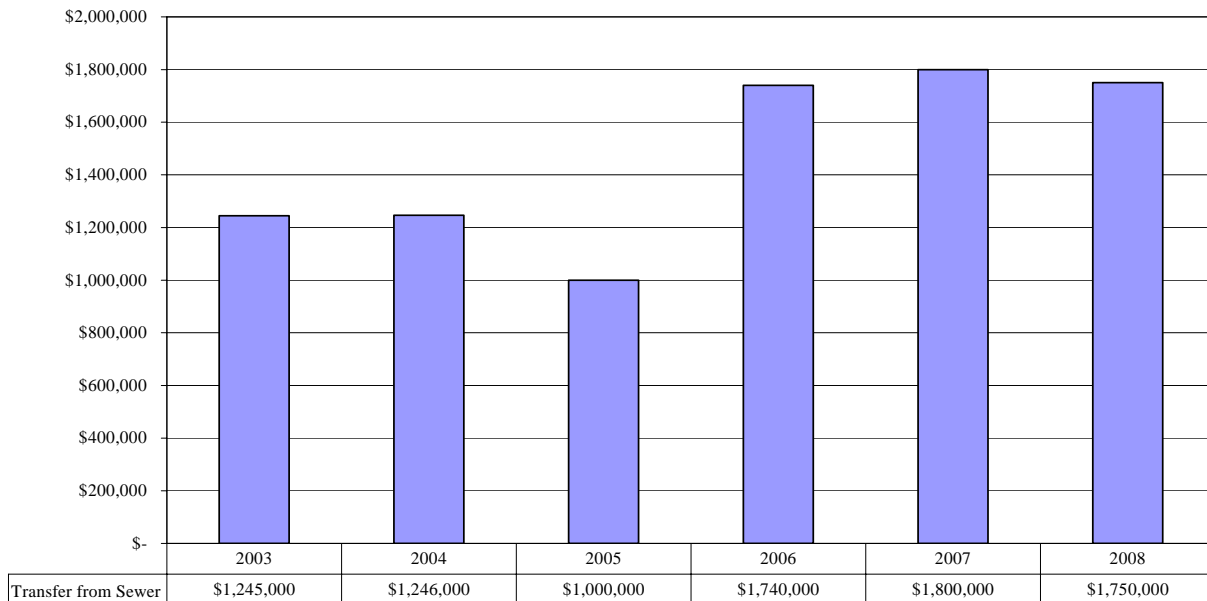
The baseline expenditure projections forecast continued rapid growth in overall expenditures. Growth is driven largely by wages; health benefits; pension costs; and refuse contract costs. Annual increases of 12.0 percent in FY2006 are projected; rising to a high of 5.6 percent in FY 2007; before increases stabilize to 3.3 percent in 2008, 2009 and 2010. Such growth factors compare with an average annual growth in City revenue of just 3.1 percent over the five years.

The PFM report then enumerated a list of recommendations necessary to address the financial dilemma. In addition, the report went on to state: “Note that even if the Mayor and Council were to adopt all of these initiatives, the City’s budget would be tenuously balanced through 2009 and would fall out of balance again in 2010.”

Operational Supplements

Operational Supplements have been used by the City of York to offset municipal expenditures during the review period. Similar to other municipalities in this study, the City of York transfers money from its Sewer Fund to cover expenditures. In 2003 the transfers of funds was approximately \$1.2 million and in 2008 the transfer was about \$1.75 million. (See Graph 8.)

Graph 8 CITY OF YORK
Operational Supplements
2003 through 2007; 2008 Budget



These transfers from the Sewer Fund are the only specific operational supplement that is readily identifiable. The City of York has a somewhat complex accounting structure with numerous interfund reimbursements including the detailed use of an Internal Service Fund. PEL believes that a detailed analysis of these reimbursements would categorize additional operational supplements beyond the sewer fund transfers.

Other Possible Operational Supplements

Over the review period the City has used interfund loans to enable certain funds to meet their financial obligations. These loans appear to be for longer than the current fiscal period and were made from the City’s business activity or enterprise funds to the City’s government activities funds. These interfund loans have grown from about \$103,000 in the 2003 audit to \$1.02 million in the 2007 audit. If such loans cannot be repaid to the originating fund, the audit

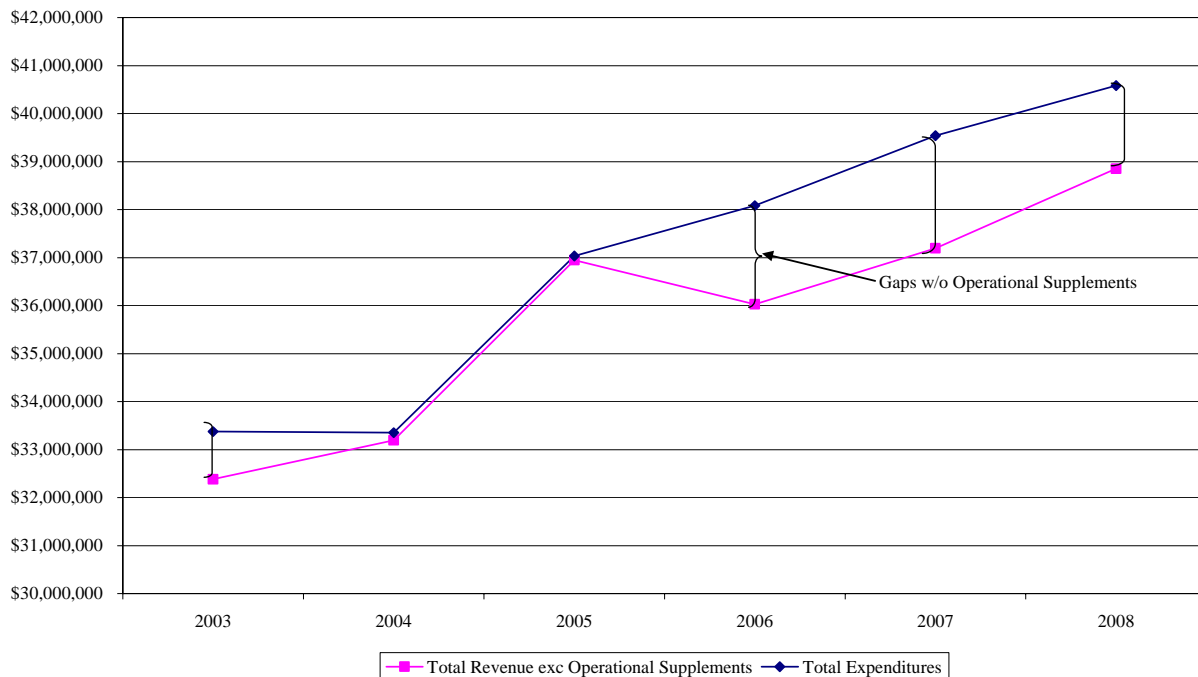
recommends that they be reclassified as transfers. As such, these transfers could be considered as operational supplements, in the same nature as the transfer from the Sewer Fund.

Table 10 and Graph 9 present Total Revenues and Total Expenditures excluding the Sewer transfer operational supplement. For the review period, if the sewer transfers are excluded from revenues, the City falls into a deficit position.

Table 10
CITY OF YORK
Total Revenues Excluding Operational Supplements vs. Total Expenditures
2003 - 2007, 2008 Budget

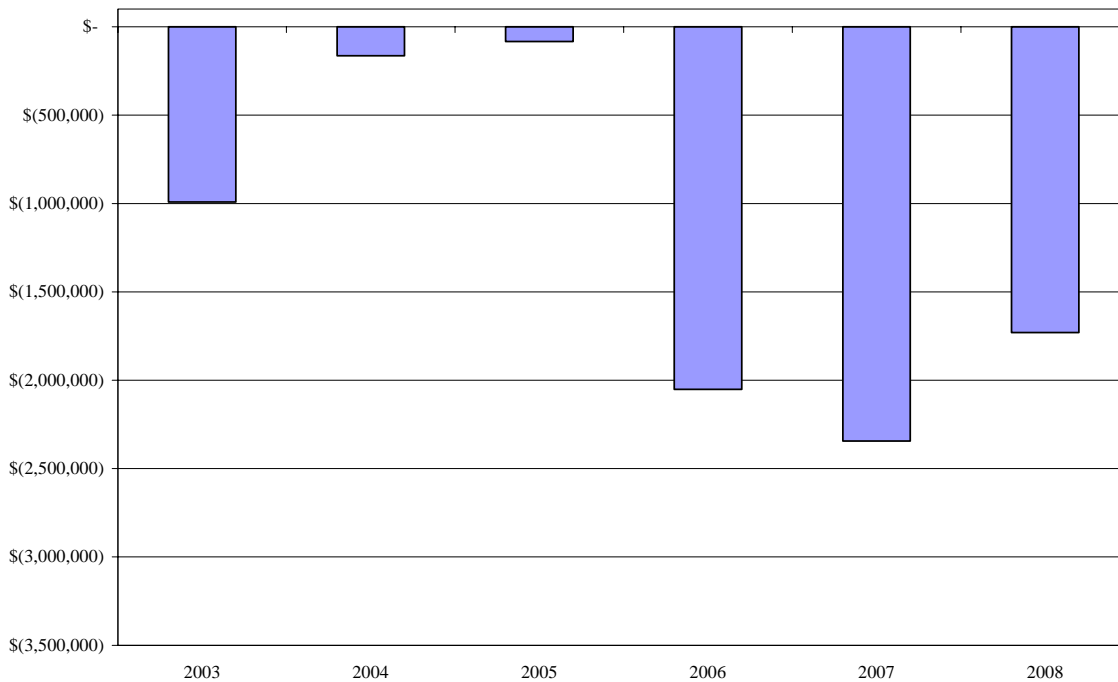
	2003 <u>Actual</u>	2004 <u>Actual</u>	2005 <u>Actual</u>	2006 <u>Actual</u>	2007 <u>Actual</u>	2008 <u>Budget</u>
Total Revenues without Operational Supplements	32,383,596	33,191,747	36,949,338	36,028,557	37,193,993	38,850,520
Total Expenditures	33,374,594	33,355,298	37,032,924	38,080,771	39,538,432	40,581,155
Surplus (Deficit)	(990,998)	(163,551)	(83,586)	(2,052,214)	(2,344,439)	(1,730,635)

Graph 9 CITY OF YORK
Revenue and Expenditures Without Supplemental Operational Revenue
2003 through 2007; 2008 Budget



For 2004 and 2005, the deficit is relatively small at \$163,551 and \$83,586 respectively. However, for the years 2006 and 2007 the deficits are substantial at \$2.05 and \$2.34 million. (See Graph 10.)

Graph10 CITY OF YORK
Deficit Without Operational Supplements
 2003 through 2007; 2008 Budget



The City of York faces significant financial issues related to increased costs that cannot be controlled without service reductions, nor met with static sources of revenues. Increasing real estate taxes on a declining assessment base puts the City at a competitive disadvantage with surrounding municipalities.

This basic problem of insufficient revenue and the inability to significantly cut expenditures without adversely affecting service levels was forcefully stated by Mayor Brenner and Mr. Michael O’Rourke, Esq., the City’s Business Administrator, in PEL’s interview for this study. Both were particularly concerned about cost escalations for Public Safety, which are beyond their control. Complicating the situation was that there were few revenue options but to raise the real estate tax millage.

Indeed Mayor Brenner related to PEL that the City has been raising millage rates in order to maintain fiscal viability but it is an uphill battle and a battle that the Mayor believes the Commonwealth’s cities are losing.

The financial constraints affecting the City have continued to grow. Mayor Benner in his 2009 budget message recounted that in the beginning of 2008 the City had only sufficient cash to pay one half of the biweekly payroll or one week of accounts payable.

The Mayor goes on to state, “What does this mean? It means that each year the City budget is much tighter; the relationship between revenue and expenditures is closer, so that we are approaching the point where we will run out of money on December 31. This is a problem to be solved because budgets are so tight that they do not provide a cushion for emergencies.”

CHAPTER 7

CITY OF EASTON

Easton is located sixty miles north of Philadelphia, and seventy miles west of New York City, at the confluence of the Lehigh and Delaware Rivers. The City is part of the Lehigh Valley metro area with Allentown and Bethlehem cities. Its population of 26,263 (2007 Census estimate) makes Easton the least populated of the five cities in the case studies. The City was a major center in the railroad and canal era and is now home to the Crayola Company and Lafayette College. Easton is also the Northampton County Seat.

Easton City Government

Incorporated as a borough in 1789, Easton became a city of the third class under the laws of the Commonwealth in 1887. From January 1972 to January, 2008 Easton operated under the Mayor-Council Optional Plan—the strong mayor form of government. As a result of a successful ballot initiative in November 2007, Easton adopted a Home Rule Charter. This significant structural change resulted from recommendations of the Early Intervention Plan (EIP) prepared by Public Financial Management and Keystone Consulting. The EIP also provided Easton with a five-year financial plan and management review audits. The Home Rule Charter reorganization allows the City to increase the Earned Income Tax rate beyond Act 511 limits and to employ a City Administrator.

In early 2008, Easton Mayor Sal Panto, Jr. announced a Clean and Safe Capital Campaign. Acknowledging that large capital projects and purchases are long-term investments that cannot be funded through the yearly budgeted General Fund, Mayor Panto re-allocated funds (approximately \$2.4 million) generated through a lease of the city's water purification plant and distribution network to the Easton Suburban Water Authority. An additional \$1.5 million from 1992 and 1998 bond issues was made available from the Capital Reserve Fund. With the exception of the purchase of an aerial truck, some of the capital items in this nearly \$4 million capital proposal were items that, in general, may have been planned and budgeted for on an annual basis. In reality, the City was “catching up” on capital improvements. Some of the capital funds available from a 2008 bond are reserved for use as matching funds for grants; other funds are reserved for recreation and public safety projects that will improve the quality of life for Easton's residents and visitors.

Easton City's Revenue Experience

Revenue for Pennsylvania cities is largely composed of property taxes and earned income taxes that rely on a taxable base of value; for property, it is the assessed values of properties in the city; for earned income it is the earnings of wage earners that reside—not work—in the city. As any tax base increases in size, the revenue to the city increases without official action. If the tax base is stagnant or declining, tax revenue does not “naturally” grow; however, governments can raise the tax millage rates on property and may be able (under certain circumstances) to raise the earned income tax rate. (See Table 1.)

Table 1
CITY OF EASTON
Real Estate Taxes, Assessed Values, Millage Rates
2003 - 2007 City Actual, 2008 Budget

	<u>Assessment</u>	<u>Millage</u>	<u>Taxes Levied</u>	<u>Taxes Collected</u>	<u>Assessed Valuation Change</u>		<u>Millage Levied Change</u>		<u>Taxes Collected Change</u>	
					<u>\$</u>	<u>%</u>	<u>Mills</u>	<u>%</u>	<u>\$</u>	<u>%</u>
2003	\$344,380,900	12.00	\$4,132,571	NA	-	-	-	-	-	-
2004	344,664,300	14.69	5,063,119	NA	-	-	2.69	22.4	-	-
2005	345,483,000	15.96	5,513,909	\$5,458,524	-	-	1.27	8.7	-	-
2006	349,310,600	18.95	6,619,436	6,595,543	3,827,600	1.1	2.99	18.7	1,137,019.48	20.8
2007	351,715,300	21.95	7,720,151	7,583,177	2,404,700	0.7	3.00	15.8	987,633.82	15.1
2008	351,928,000	24.95	8,780,604	6,541,074	212,700	0.1	3.00	13.7	(1,042,103.29)	(13.7)
Change 2003-2007										
\$	\$7,334,400	9.95	\$3,587,580	-	-	-	-	-	-	-
%	2.1%	82.9%	86.8%	-	-	-	-	-	-	-

NA = Not Available

SOURCE: Easton City

Special Fund Accounting

A brief comment needs to be made regarding the treatment of tax receipts by the City of Easton. The City levies separate millage rates for both general purposes and debt service and accounts for these real estate taxes in separate funds—the General Fund and Debt Service Fund. To get a proper measure of the City’s total tax situation, PEL combined the revenues of these funds into one fund. To keep the measurement balanced, expenditures for the funds were also totaled into one fund. The data used for this purpose was gathered from the unaudited City General Fund reports and from the City’s audits for Debt Service Fund.

Earned Income Tax

Easton had an Earned Income Tax (EIT) rate of 0.5 percent prior to 2009. For the review period 2005 through 2008, the City’s EIT collections have averaged \$1.79 million yearly. Based upon the period 2005 through 2008 the EIT increased by \$178,908 or 10.7 percent from 2005 through 2008. (See Table 2.)

Table 2
CITY OF EASTON
Earned Income Tax
2005 - 2007 Actual, 2008 Budget

<u>Year</u>	<u>%Rate</u>	<u>Total EIT Taxes</u>	<u>Change</u>	
			<u>\$</u>	<u>%</u>
2005	0.5	\$1,671,092	-	-
2006	0.5	1,760,759	89,668	5.4
2007	0.5	1,868,678	107,919	6.1
2008 Budget	0.5	1,850,000	-18,678	-1.0
Change 2005-2008				
	\$	\$178,908		
	%	10.7%		
Average 2005-2008		\$1,787,632		

SOURCE: Easton City.

The City’s recently adopted Home Rule Charter permits the City to raise the rates of certain taxes above the normal limits for municipalities that operate without home rule authority. Easton has increased the resident EIT rate by 0.75 percent (to a total tax rate of 1.25 percent) for the 2009 fiscal year.

Taxes and Other Revenue

During the period 2003 through 2008, total revenue has increased from \$26.2 million in 2005 to \$28.9 million for the 2008 budget estimate, a \$2.7 million or 10.3 percent change over the period. Real Estate Taxes grew by \$3.3 million or 60.4 percent over the period.

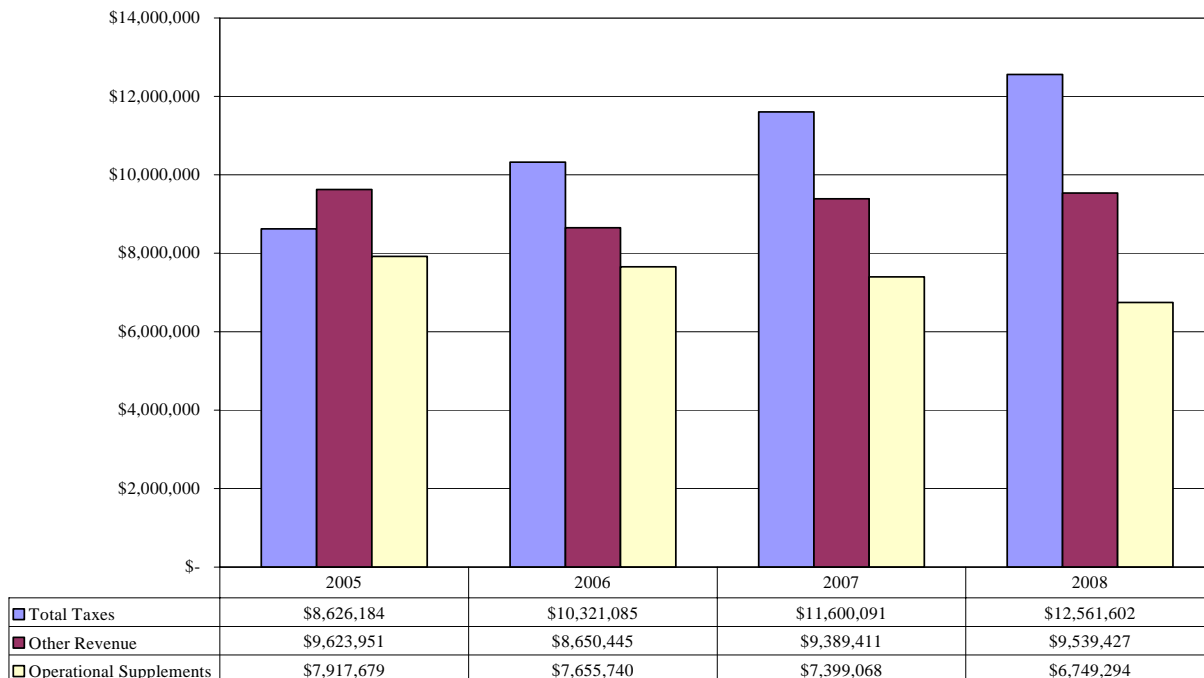
There has been a steady growth in total taxes over the period 2003 through budget 2008. The “Other Taxes” category was down slightly in 2008 due to the Commonwealth’s legislative

change in procedure for the collection of the Local Services Tax. The “Other Revenue” category varied during the period, ranging from \$8.6 million in 2006 to \$9.6 million in 2005. The “Operational Supplements” category has decreased from a high of \$7.9 million in 2005 to a projected \$6.7 million for budget 2008. In 2005 and 2006 the City sold assets valued at approximately \$1.0 million which contributed to the operational supplements category. Overall, total revenues from 2005 through budget 2008 grew by 10.3 percent. (See Table 3 and Graph 1.)

Table 3
CITY OF EASTON
Revenue Components
2005 - 2007, 2008 Budget

	2005 <u>Actual</u>	2006 <u>Actual</u>	2007 <u>Actual</u>	2008 <u>Budget</u>	<u>Change 2005 -2008</u>	
Real Estate Taxes	\$ 5,458,524	\$6,595,543	\$7,583,177	\$8,757,502	\$3,298,978	60.4%
All Other Taxes	3,167,660	3,725,541	4,016,914	3,804,100	636,440	20.1
Other Revenue	9,623,951	8,650,445	9,389,411	9,539,427	-84,524	-0.9
Operational Supplements	<u>7,917,679</u>	<u>7,655,740</u>	<u>7,399,068</u>	<u>6,749,294</u>	<u>-1,168,385</u>	-14.8
Total Revenue	\$26,167,815	\$26,627,269	\$28,388,570	\$28,850,323	\$2,682,508	10.3%

Graph 1 CITY OF EASTON
Taxes; Other Revenue; Operational Supplements
2005 through 2007 Reported; 2008 Budget



The Expenditure Experience of the City of Easton

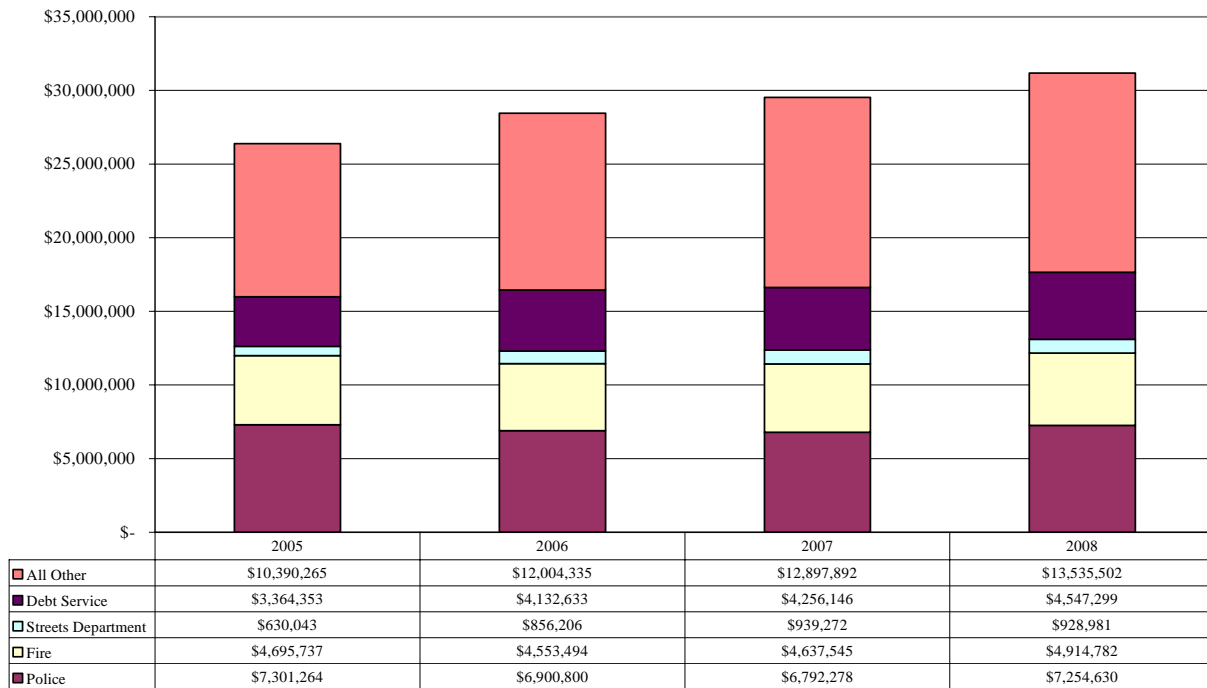
Table 4 provides a summary of expenditures for the City of Easton from 2005 through the 2008 budget estimate. Expenditure categories include the General Fund and the Debt Service Fund, these funds that have tax dollars as part of the revenue source. (While revenue data was available for the 2003-2008 period, expenditure data was only available for 2005-2008 as a result of a change in the method of accounting in 2005.)

Table 4
CITY OF EASTON
Expense Components
2005 to 2008 Budget

	<u>2005</u> <u>Actual</u>	<u>2006</u> <u>Actual</u>	<u>2007</u> <u>Actual</u>	<u>2008</u> <u>Budget</u>	<u>Change 2005 -2008</u>	
Police	\$ 7,301,264	\$ 6,900,800	\$ 6,792,278	\$ 7,254,630	\$ -46,634	-0.6%
Fire	4,695,737	4,553,494	4,637,545	4,914,782	219,045	4.7
Streets Department	630,043	856,206	939,272	928,981	298,938	47.4
Debt Service	3,364,353	4,132,633	4,256,146	4,547,299	1,182,946	35.2
All Other	<u>10,390,265</u>	<u>12,004,335</u>	<u>12,897,892</u>	<u>13,535,502</u>	<u>3,145,237</u>	30.3
Total Expenditures	\$26,381,663	\$28,447,467	\$29,523,133	\$31,181,194	\$4,799,531	18.2%

Total expenditures have increased from \$26.4 million in 2005 to \$31.2 million for the 2008 budget estimate, a \$4.8 million or 18.2 percent increase. Over the review period, significant increases were experienced in the Streets Department, \$298,000 or 47.4 percent; Debt Service \$1.2 million or 35.2 percent and All Other Expenses, \$3.1 million or 30.3 percent. The majority of the Debt Service increase is related to the 2007 Pension Bond issue of \$15,646,000 and to a 2005 series of \$9,360,000. The Other Expenditures category includes expenditures for refuse collection and sewer expense. It should be noted that in 2007, the City refunded the 1996 Pension Bond Issue principal of \$16,076,000 and issued the 2007 Pension Bond in the amount of \$16,065,000. In accordance with Act 205, the State Retirement Commission authorized the City of Easton to participate as a level three distressed community which requires aggregating all pension funds into a single pension fund. (See Graph 2.)

Graph 2 CITY OF EASTON
Expenditure Components
 2005 through 2007; 2008 Budget

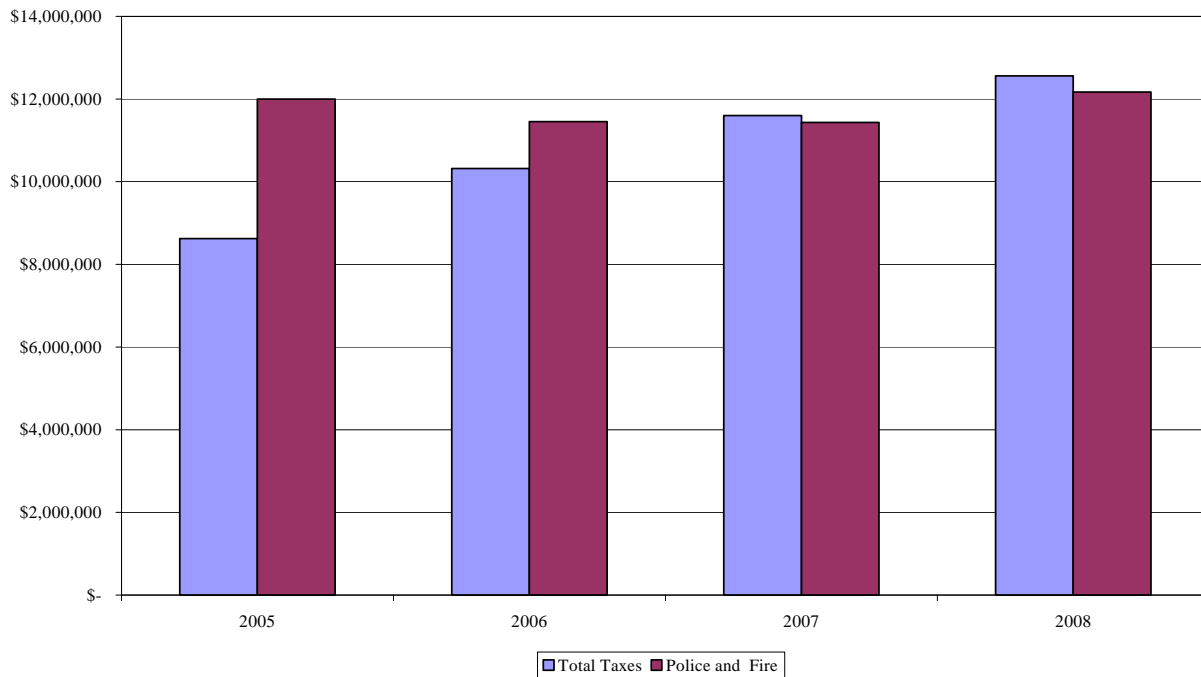


Total Taxes vs. Police and Fire Expenditures

Fire expenditures showed moderate increases throughout the period increasing by \$219,045 or 4.7 percent. Police expenditures decreased by \$508,986 from 2005 through 2007 but are estimated to increase in 2008 by \$462,000 over 2007.

Police and fire expenditure changes can also be measured against all other expenditures including debt service. In 2005 police and fire were 83.4 percent of all other expenditures; by 2008 Police and Fire were 64.0 percent of all other expenditures. (See Graph 3.)

Graph 3 CITY OF EASTON
Police and Fire Expenditures Compared to Total Taxes
2005 through 2007; 2008 Budget

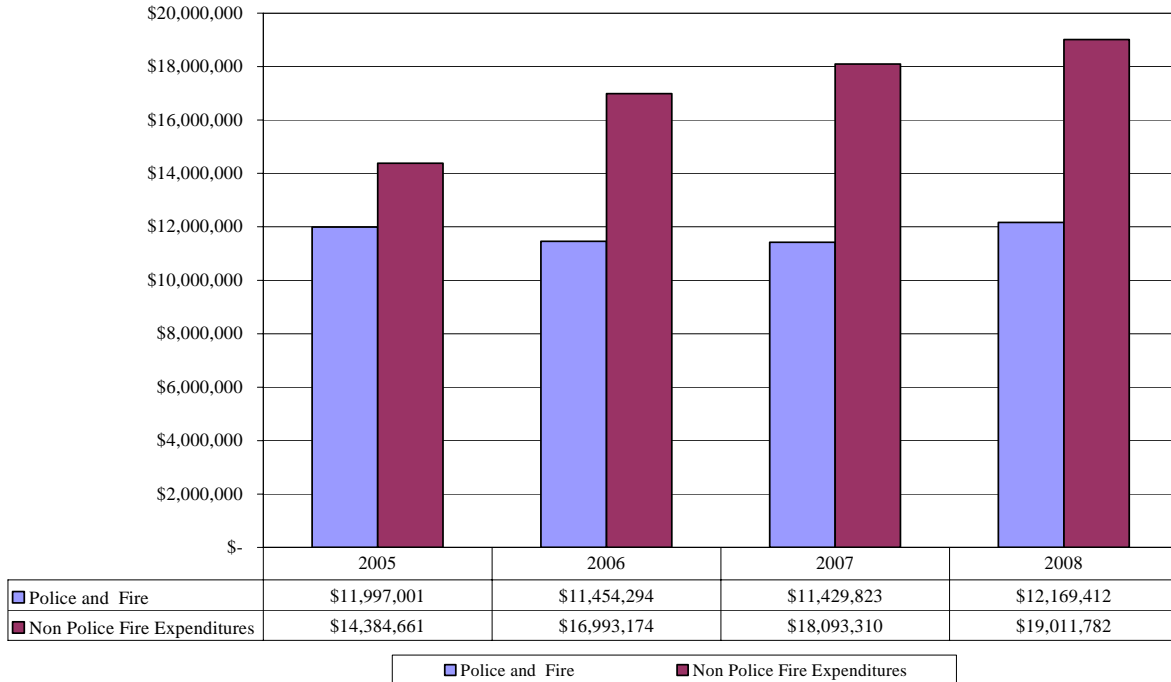


Taxes have historically provided the revenue stream to fund the bulk of local government services and citizens generally believe that their taxes pay for all the government services they require. Table 5 and Graph 4 depict total taxes compared to police and fire expenditures for 2005 through 2008 budget.

Table 5
CITY OF EASTON
Police and Fire Expenditures Compared to Total Taxes
2005 - 2007, 2008 Budget

	2005 <u>Actual</u>	2006 <u>Actual</u>	2007 <u>Actual</u>	2008 <u>Budget</u>
Total Taxes	\$8,626,184	\$10,321,085	\$11,600,091	\$12,561,602
Police and Fire Expenditures	11,997,001	11,454,294	11,429,823	12,169,412
Total Taxes Over (Under)	\$(3,370,818)	\$(1,133,209)	\$170,269	\$392,190
Police and Fire Expenditures as a Percentage of Total Taxes	139.1%	111.0%	98.5%	96.9%

Graph 4 City of EASTON
Police and Fire Compared to All Other Expenditures
2005 through 2007; 2008 Budget



Included in total taxes are the revenues received each year from the City’s debt service millage. When debt service is removed from total real estate tax receipts, the gap between receipts and police and fire expenditures is noticeably significant. (See Table 6.)

Table 6
CITY OF EASTON
Police and Fire Expenditures Compared to
Total Taxes Less Debt Service Real Estate Taxes
2005 - 2007, 2008 Budget

	2005 <u>Actual</u>	2006 <u>Actual</u>	2007 <u>Actual</u>	2008 <u>Budget</u>
Total Taxes Less Debt Service Tax	\$ 7,397,378	\$ 8,936,224	\$ 9,440,097	\$10,345,174
Police and Fire Expenditures	11,997,001	11,454,294	11,429,823	12,169,412
Total Taxes Less Debt Service Tax Over (Under) Police and Fire Expenditures	(4,599,623)	(2,518,070)	(1,983,726)	(1,824,238)

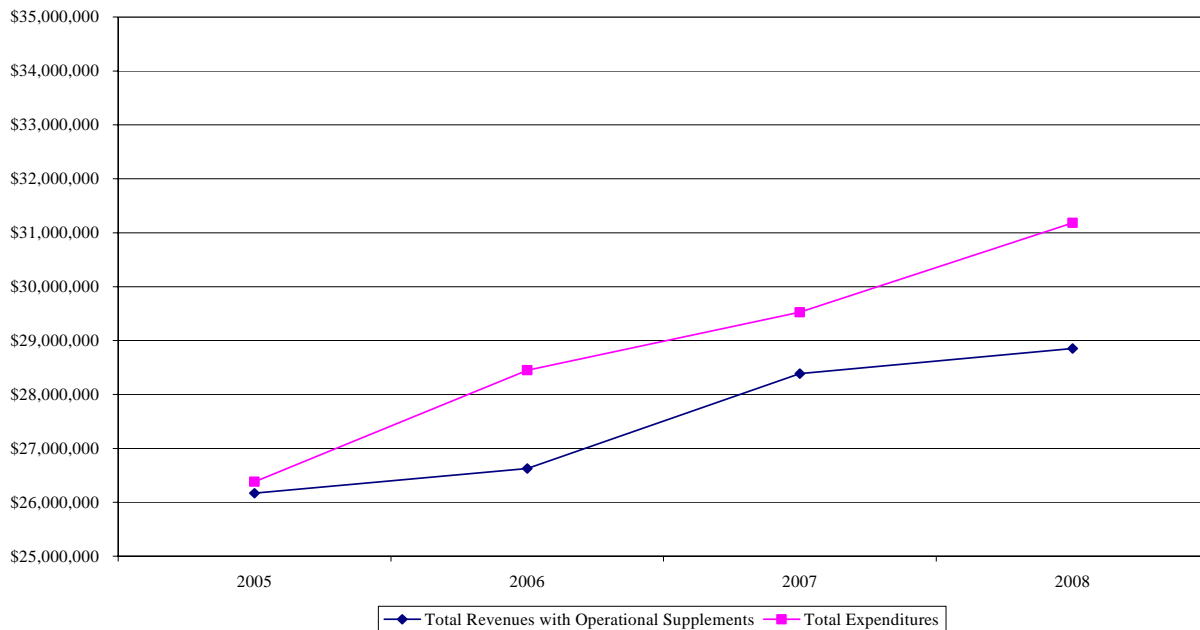
Total Revenues and Expenditures

Table 7 presents Total Revenues with operational supplements and Expenditures for the City of Easton for the General Fund and the Debt Service Fund for 2005 through the 2008 budget. For 2005 through 2008, total expenditures were greater than total revenues. (See Graphs 5 and 6.)

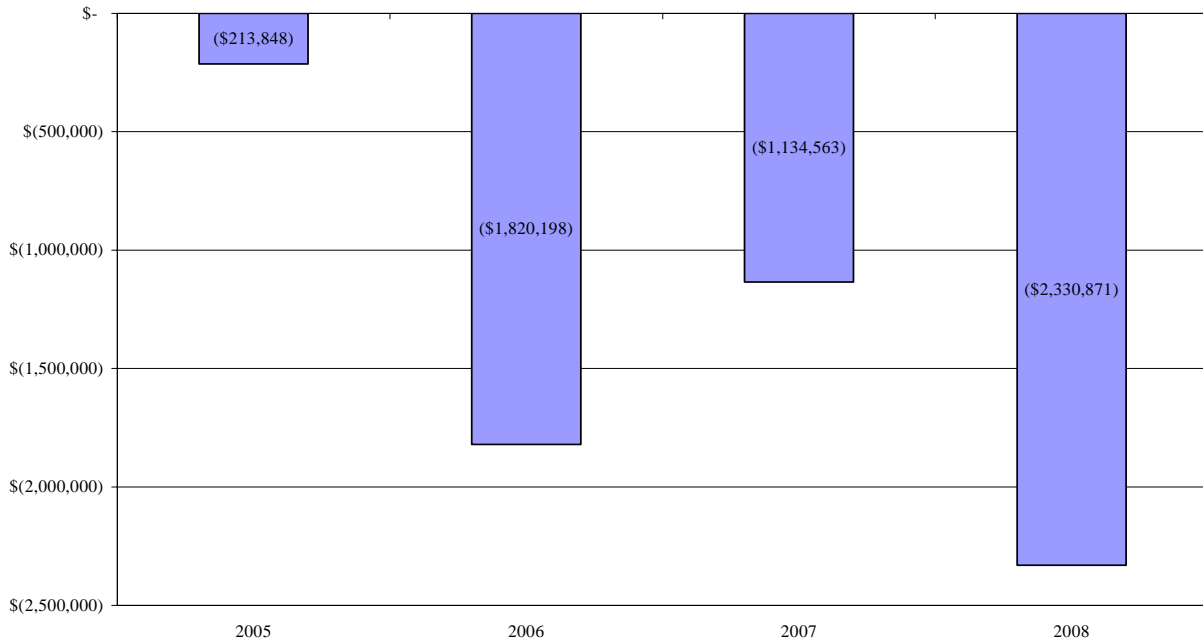
Table 7
 CITY OF EASTON
 Total Revenues with Operational Supplements vs. Total Expenditures
General Fund and Debt Service Fund
 2005 - 2007, 2008 Budget

	2005 <u>Actual</u>	2006 <u>Actual</u>	2007 <u>Actual</u>	2008 <u>Budget</u>
Total Revenues with Operational Supplements	\$26,167,815	\$26,627,269	\$28,388,570	\$28,850,323
Total Expenditures	26,381,663	28,447,467	29,523,133	31,181,194
Surplus (Deficit)	(213,848)	(1,820,198)	(1,134,563)	(2,330,871)

Graph 5 CITY OF EASTON
Revenues With Operational Supplements and Expenditures
 2005 through 2007; 2008 Budget



Graph 6 CITY OF EASTON
Surplus (Deficit)
 2003 through 2007; 2008 Budget
Includes All Operational Supplement Funds



Operational Supplements

Operational Supplements have been used by the City of Easton to pay for operating expenditures during the review period. Easton uses revenues from its sewer and water operations to transfer revenue to the General Fund. Easton accounts for the Sewer Operations in its General Fund and the net of Sewer Revenues less Sewer Expenses are depicted as an Operational Supplement from sewer revenue. In addition, Easton receives income from the Water System of approximately \$2.1 million per year. (See Graph 7.)

Graph 7 CITY OF EASTON
Operational Supplements
2005 through 2007; 2008 Budget

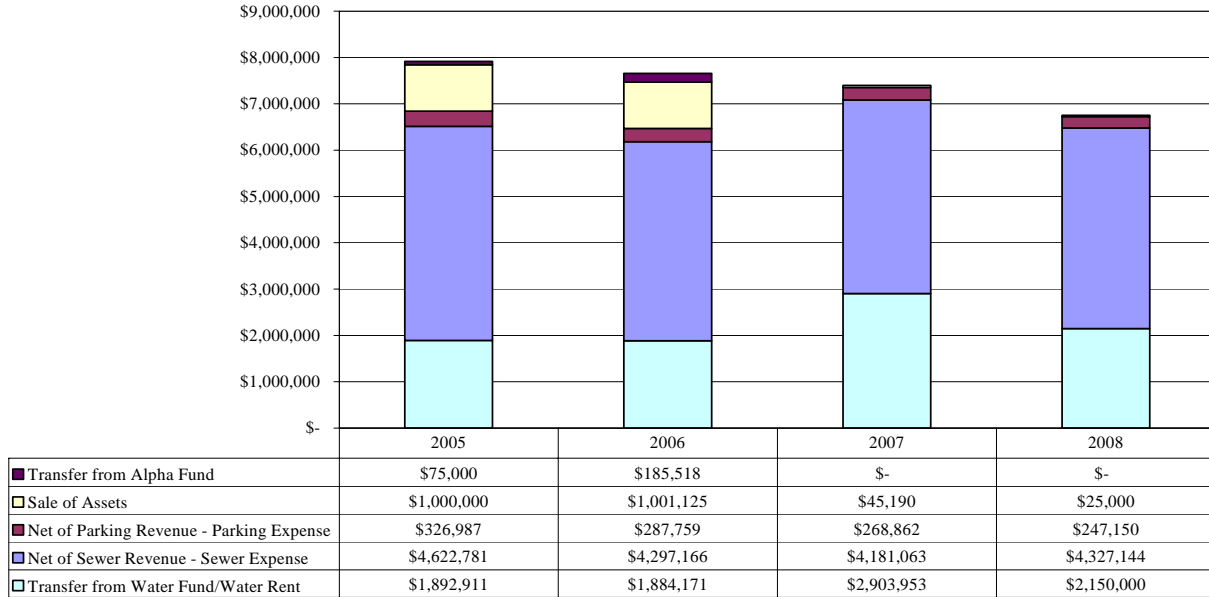


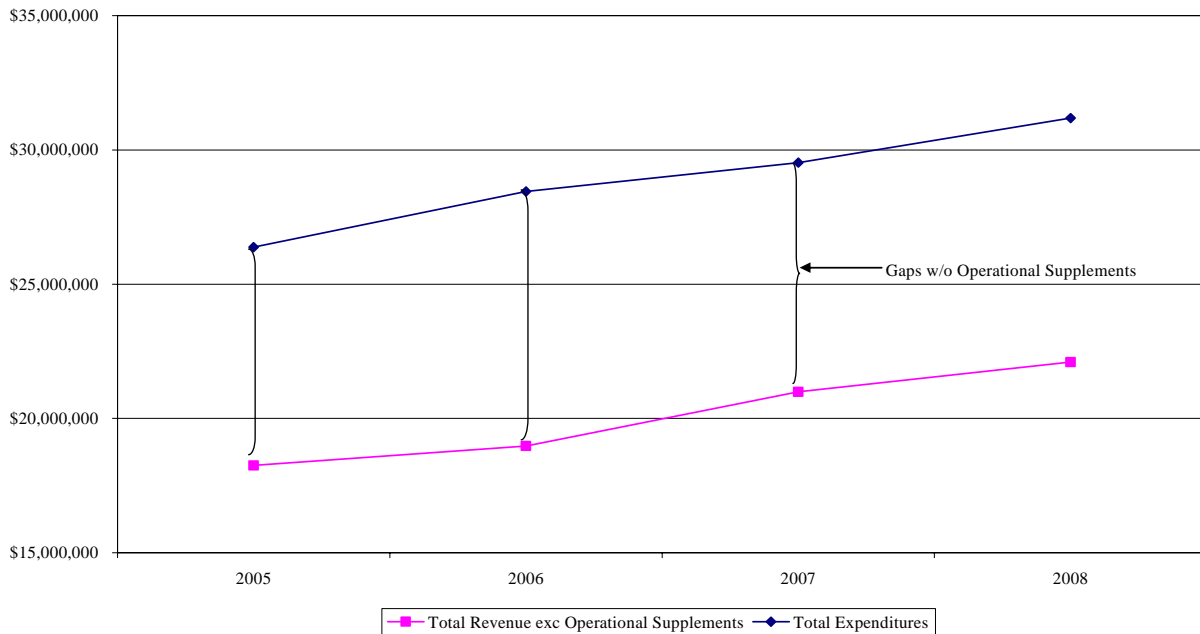
Table 8 and Graphs 8 and 9 depict the City’s financial position in the absence of operational supplements. Clearly without these additional revenue sources the City would be in a financial position of extreme difficulty.

The increase in the EIT rate for 2009 and beyond will provide the City with estimated additional revenue of \$2.7 million per year. However, based upon historical collection patterns observed in other municipalities, this additional revenue will take up to eighteen months to be fully realized by to the City. While the additional levy will be utilized for the 2009 and 2010 budget, the City’s current deficit balance (without optional supplements) will be reduced but not eliminated by this new tax levy.

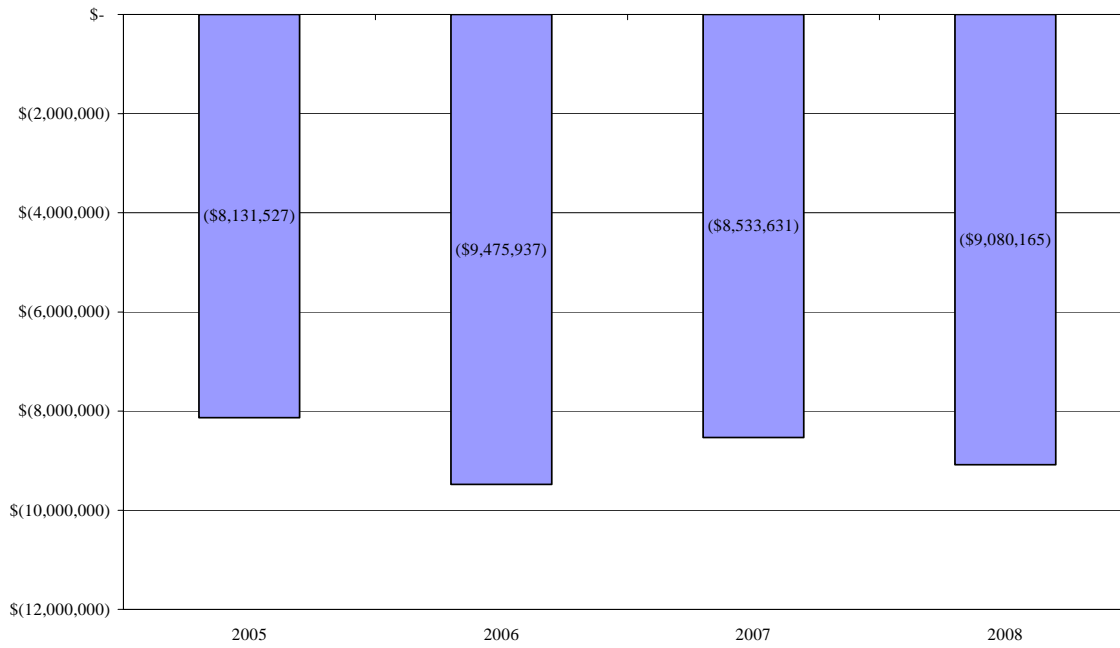
Table 8
CITY OF EASTON
Total Revenues Excluding Operational Supplements vs. Total Expenditures
2005 - 2007, 2008 Budget

	2005 <u>Actual</u>	2006 <u>Actual</u>	2007 <u>Actual</u>	2008 <u>Budget</u>
Total Revenues without Operational Supplements	\$18,250,135	\$18,971,530	\$20,989,502	\$22,101,029
Total Expenditures	26,381,663	28,447,467	29,523,133	31,181,194
Surplus (Deficit)	\$(8,131,527)	\$(9,475,937)	\$(8,533,631)	\$(9,080,165)

Graph 8 CITY OF EASTON
Revenue and Expenditures Without Supplemental Operational Revenue
2003 through 2007; 2008 Budget



Graph 9 CITY OF EASTON
Deficit Without Operational Supplements
2005 through 2007; 2008 Budget



CHAPTER 8

COMPARATIVE REVIEW

Based on the previous profiles it is evident that among these case study municipalities there are substantive demographic, sociological, and governmental differences. In addition, these municipalities provide a variety of both different services and service levels paid for by alternative methods of financing and accounting for these operations.

While the cities have different demographics and financial requirements, they share the challenge of providing the basic public services by relying on existing allowable revenue streams. On the expenditure side each municipality expends its largest share of resources maintaining the most fundamental services of police and fire protection.

On a larger scale, it also has been demonstrated that each of the municipal governments has been engaged in using—to varying degrees—operational supplements in order to bring total revenues into balance with total expenditures. In simple terms, the case study municipalities try to find other resources each year “to plug” their revenue gap. This chapter attempts to tie together these operational supplements along with other financial factors common to the case study municipalities.

Given the variances in the dollar size of both revenue and expenditures among the entities, it is necessary to standardize the financial values to produce a common measure. PEL has elected to use population as the common denominator. Thus, for the most part, revenue and expenditure parameters are measured by categories of per capita, e.g. real estate taxes per capita, police and fire expenditures per capita. PEL has used the average of the 2000 Census population and the estimated 2007 population for each municipality. (See Table 1.)

Table 1
POPULATION
2000 Actual , 2007 Estimate, Average

	2000	2007	Average
Bethlehem	71,329	72,531	71,930
Easton	26,263	26,094	26,179
Lancaster	56,348	54,672	55,510
Reading	81,207	80,769	80,988
York	40,861	40,226	40,544

SOURCE: 2000 U.S. Census, 2007 Census Estimates

Real Estate Taxes

Taxable Property Base

Taxable market values for 2007 range from \$679,580,800 in Easton City to \$2,820,241,700 in Bethlehem, a multiple of four times in relative market value. (See Table 2.)

Table 2
MARKET VALUE
2003 to 2007

<u>Year</u>	<u>Bethlehem</u>	<u>Easton</u>	<u>Lancaster</u>	<u>Reading</u>	<u>York</u>
2003	\$2,221,788,800	\$535,899,000	\$1,359,540,400	\$1,174,396,400	\$732,989,600
2004	2,407,360,700	584,388,200	1,434,087,600	1,209,538,800	768,884,800
2005	2,426,637,600	586,201,900	1,436,676,800	1,206,414,200	767,365,700
2006	2,774,175,100	673,789,000	1,606,197,100	1,309,931,000	810,598,400
2007	2,820,241,700	679,580,800	1,621,820,300	1,308,441,200	805,653,500
Per Capita	\$35,174	\$23,377	\$26,872	\$15,332	\$19,167

SOURCE: State Tax Equalization Board

The per capita market values, based upon a five-year average, range from \$15,332 in Reading to \$35,174 in Bethlehem. Reading with the largest population has the lowest per capita taxable market value, while Bethlehem’s second highest population of 71,930 has the highest market value per capita in the review group. (See Graph 1.)

Table 3 provides the dollar and percentage changes for market value assessments in each municipality for the period 2003 through 2007. On a dollar basis, the yearly change in market value can vary widely. On a percentage basis, the change of market value over the base year of 2003 shows a more gradual change. The average yearly change in market values for the period 2003-2007 was 6.7 percent for Bethlehem and Easton (located in the same county), 4.8 percent for Lancaster, 2.8 percent for Reading and 2.5 percent for York.

Graph 1
PER CAPITA AVERAGE MARKET VALUE
 2003 - 2007

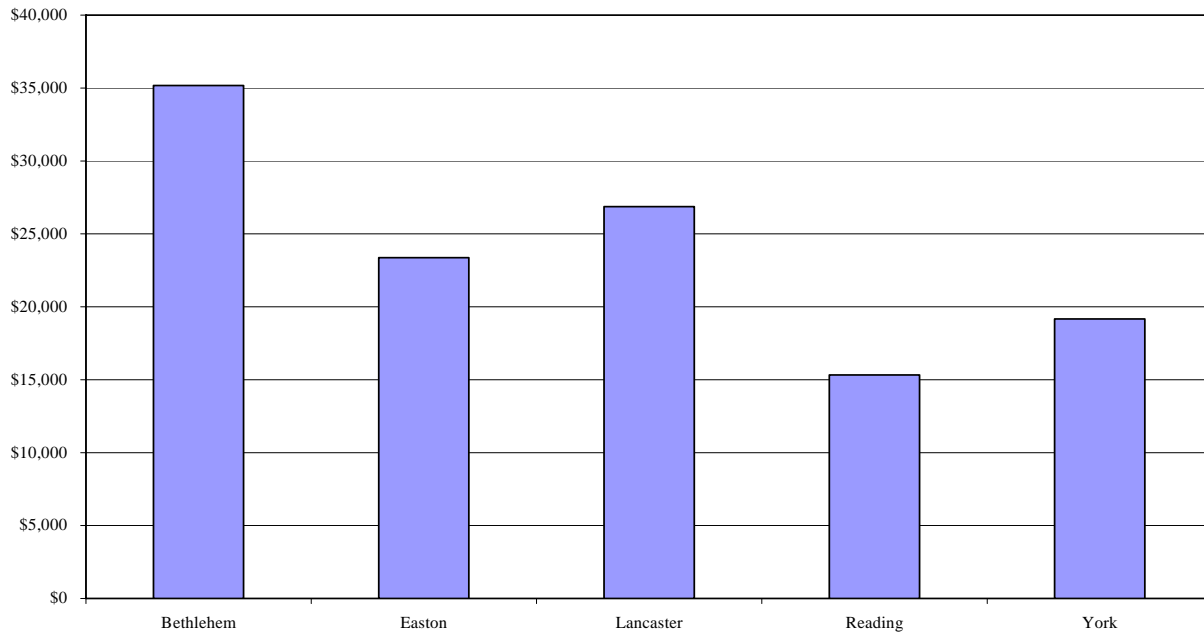


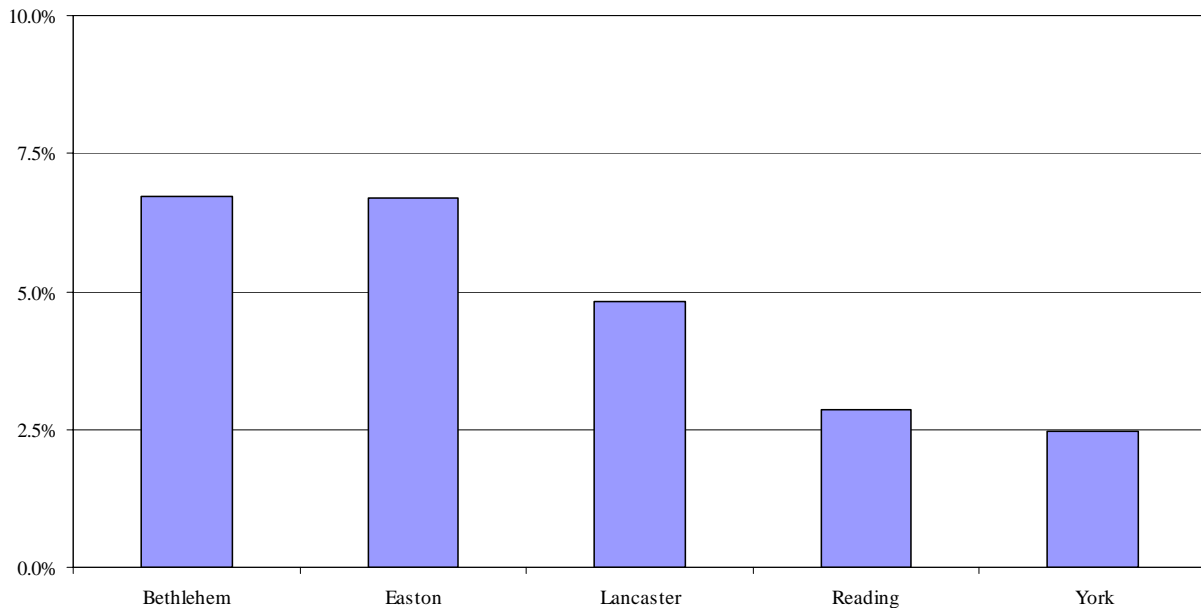
Table 3
CHANGE IN MARKET VALUE
 2003 – 2007 Actual

	CHANGE FROM PREVIOUS YEAR									
	Bethlehem		Easton		Lancaster		Reading		York	
	\$	%	\$	%	\$	%	\$	%	\$	%
2003-04	185,571,900	8.4	48,489,200	9.0	74,547,200	5.5	35,142,400	3.0	35,895,200	4.9
2004-05	19,276,900	0.8	1,813,700	0.3	2,589,200	0.2	-3,124,600	-0.3	-1,519,100	-0.2
2005-06	347,537,500	14.3	87,587,100	14.9	169,520,300	11.8	103,516,800	8.6	43,232,700	5.6
2006-07	46,066,600	1.7	5,791,800	0.9	15,623,200	1.0	-1,489,800	-0.1	-4,944,900	-0.6
Avg. Yearly Change	149,613,225	-	35,920,450	-	65,569,975	-	33,511,200	-	18,165,975	-
Avg. Change vs. 2003 Base	-	6.7	-	6.7	-	4.8	-	2.8	-	2.5

Market values are reflected in the taxable assessed valuation as a tax base available to the city for real estate taxation. There is often a time lag for changes to assessed valuation from increased market values, but a change of less than 7.0 percent for a five-year period would not produce a large enough increase in assessed valuation for significant growth in taxation, even

without the normal lag in capturing growth in market value. If a county does not have a new reassessment, older municipalities will not capture growth in market values in a consistent and timely manner and property tax revenue will be reduced as a result. (See Graph 2.)

Graph 2
AVERAGE PERCENTAGE CHANGE IN MARKET VALUE
 2003-2007



As the relationship of market value to assessed values changes over time, increases in the assessed value are lagged in time and the expected increases in a municipal tax base are delayed, sometimes for many years. This delay demonstrates why economic development and growth (by themselves) do not immediately produce increased real estate tax revenue for a city.

Nontaxable Property Valuations

Property exempt from taxation reduces the taxable assessed valuation. The 2008 percentage of nontaxable property assessment for Bethlehem was 19.4 percent of its total assessed value; for Easton, 26.8 percent; for Lancaster, 23.6 percent; for Reading, 26.8 percent; and York, 37.5 percent.

The nontaxable property includes schools, colleges, hospitals, churches, other charitable entities as well as governmental owned property. Although providing a social benefit to the

entire area (not just the host municipality) these nontaxable properties create a loss of revenue from the total real estate tax base and have been an issue of major concern for the municipalities. Various legislative initiatives have been proposed to remedy the problem but, as of this report, none have been passed.

A solution implemented to address this problem is for the municipality to request payments in lieu of taxes, (PILOTS) from the nontaxable entities. Each of the case study municipalities has some program or systematic approach to achieve these payments but only in Lancaster City is there a significant payment amount. More commonly, PILOTS are voluntary and are often based on a yearly agreement which precludes relying on the receipt of money over an extended period of time.

Real Estate Taxes

The rate of real estate taxation (millage) is given for each municipality in Table 4. For Bethlehem, Easton, Reading, and York millages increased (for the most part in almost every year) during the review period. For Lancaster there was a decrease between 2004 and 2005 (from 8.24 to 7.67 mills) as a result of the 2005 countywide reassessment. After 2005, the millage for Lancaster continued to increase. In Bethlehem, millages were unchanged from 2007 to 2008; in Reading millages remained the same from 2003 through 2005. It should also be noted that the City of Reading's Home Rule Charter caps real estate tax increases for any year at a maximum of five percent. (A recent court ruling may have removed the use of millage limits under the Home Rule Charter.) The Reading School District, which is coterminous with the City, increased the EIT in the school district under the terms of Act 1 of 2006, and reduced the school real estate tax rate. The reduction in school district real estate taxes did not permit the city to access this tax base since the school district reduction applied only to the homestead exemption for school purposes. (See Table 4.)

Table 4
MILLAGE RATES
 2003 - 2007 Actual, 2008 Budget

Year	MILLAGE RATES				
	Bethlehem	Easton	Lancaster	Reading	York
2003	11.500	12.000	8.240	10.300	11.390
2004	11.750	14.690	8.240	10.300	12.520
2005	12.500	15.960	7.670	10.300	13.520
2006	13.960	18.950	8.170	10.400	13.170
2007	14.100	21.950	8.820	10.900	13.670
2008 Budget	14.100	24.950	9.180	10.900	14.670
Average	13.282	19.300	8.416	10.560	13.510
Change 2003 to 2008 Budget					
Mills	2.600	12.950	0.940	0.600	3.280
Percent	22.6	107.9	11.4	5.8	28.8

SOURCE: Respective Cities.

Real Estate Taxes Per Capita

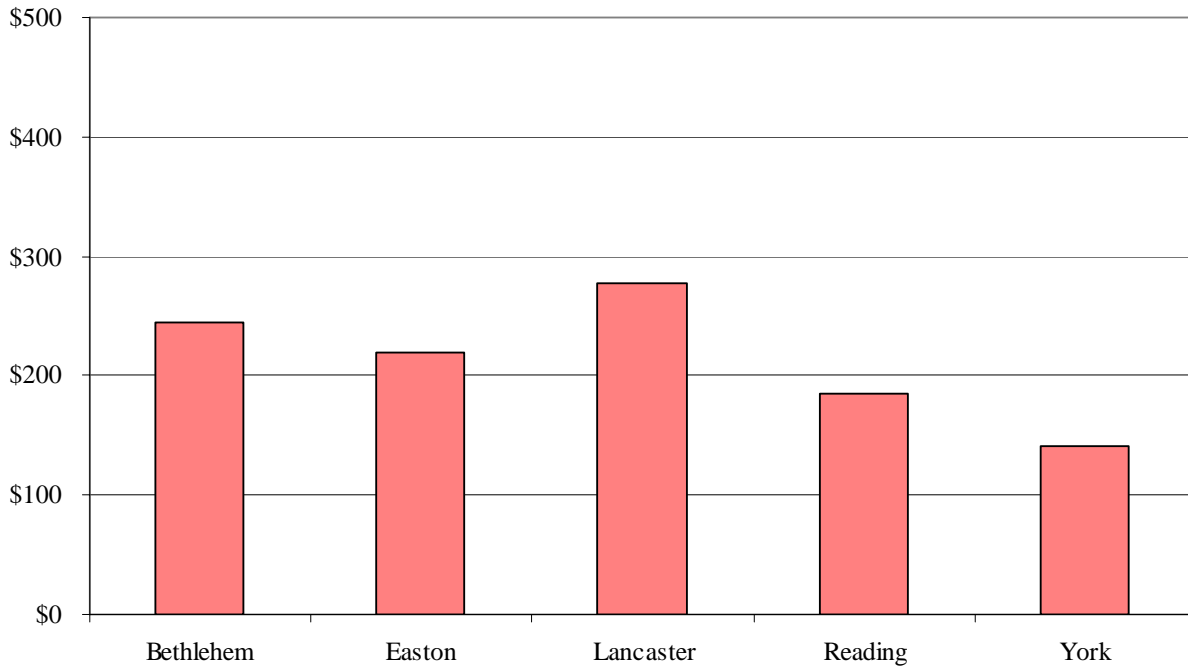
The Real Estate Tax revenue per capita for each municipality is shown in Table 5. The average per capita real estate tax ranged from \$141.75 in York to \$278.06 in Lancaster. (See Table 5 and Graph 3.)

Table 5
REAL ESTATE TAXES PER CAPITA
 2003 - 2007 Actual, 2008 Budget

Year	REAL ESTATE TAXES PER CAPITA				
	Bethlehem	Easton	Lancaster	Reading	York
2003	\$208.96	\$ 85.80	\$260.09	\$180.67	\$110.52
2004	212.92	143.67	256.71	180.64	120.93
2005	233.85	208.51	263.98	185.16	147.37
2006	261.96	251.95	278.26	187.11	153.70
2007	271.10	289.67	296.93	189.96	158.77
2008 Budget	281.99	334.53	312.39	190.53	159.21
Average	\$245.13	\$219.02	\$278.06	\$185.68	\$141.75
Change 2003 to 2008 Budget					
\$	\$73.03	\$248.73	\$52.31	\$9.86	\$48.69
%	34.9%	289.9%	20.1%	5.5%	44.0%

SOURCE: Respective Cities.

Graph 3
AVERAGE REAL ESTATE TAXES PER CAPITA
 2003-2007 Actual, 2008 Budget

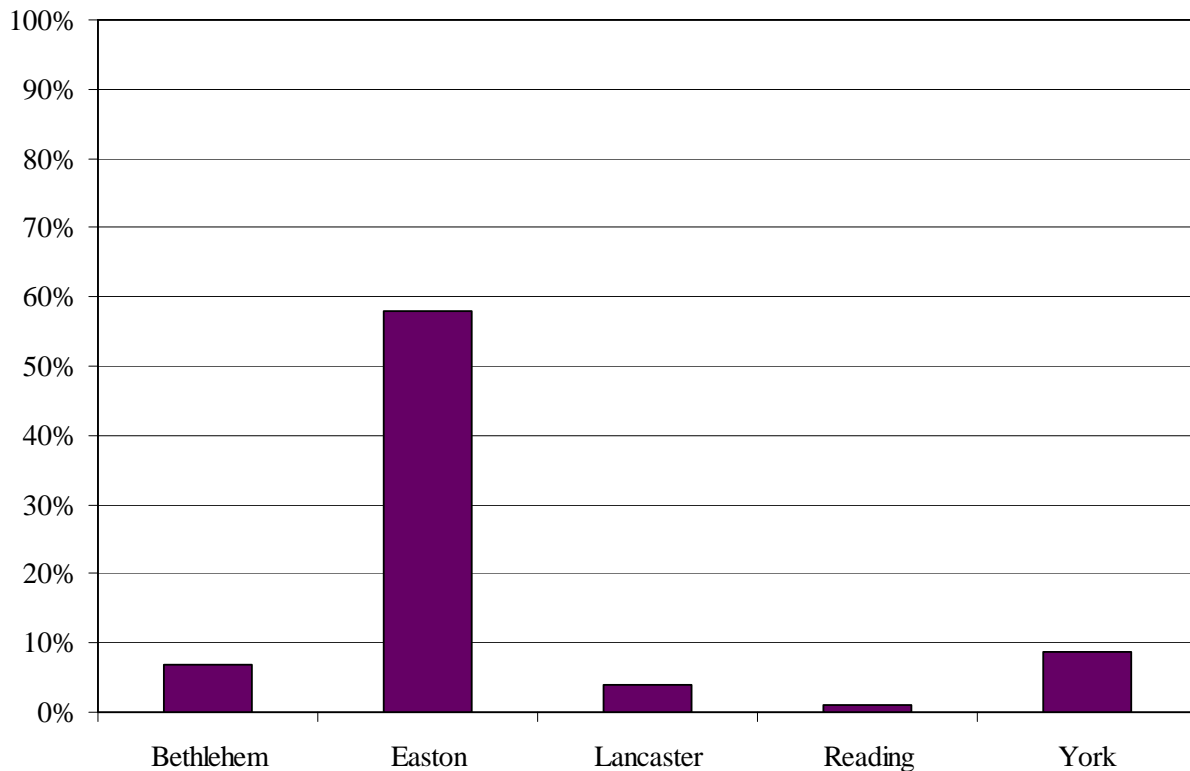


Although the per capita real estate tax revenue differs among the review municipalities, in all but one (Lancaster City, 2003 to 2004) the tax revenue for the individual municipality has increased over the prior year. The percentage increase of the per capita real estate tax increased in each city ranging from 1.1 percent in Reading to 58.0 percent in Easton. (See Table 6 and Graph 4.)

Table 6
CHANGE IN REAL ESTATE TAXES PER CAPITA
 2003 – 2007 Actual, 2008 Budget

	CHANGE FROM PREVIOUS YEAR									
	Bethlehem		Easton		Lancaster		Reading		York	
	\$	%	\$	%	\$	%	\$	%	\$	%
2003-04	3.97	1.9	57.87	67.5	-3.38	-1.3	-0.03	<-0.1	10.40	9.4
2004-05	20.92	9.8	64.84	45.1	7.27	2.8	4.53	2.5	26.44	21.9
2005-06	28.12	12.0	43.43	20.8	14.28	5.4	1.95	1.1	6.33	4.3
2006-07	9.13	3.5	37.73	15.0	18.67	6.7	2.84	1.5	5.08	3.3
2007-08	10.89	4.0	44.86	15.5	15.47	5.2	0.57	0.3	0.44	0.3
Avg. Yearly Change	14.61	-	49.75	-	10.46	-	1.97	-	9.74	-
Avg. Change vs. 2003 Base	-	7.0	-	58.0	-	4.0	-	1.1	-	8.8

Graph 4
AVERAGE PERCENT CHANGE IN PER CAPITA REAL ESTATE TAXES
 2003-2008



Total Taxes

Historically real estate taxes have been the foundation of total municipal taxation. Total taxes also include earned income taxes and other Act 511 taxes.

York City, during the period 2003 through the 2008 budget, had the highest average total taxes per capita at \$441.85, followed by Bethlehem, \$386.42, and Lancaster and Reading at \$385.24 and \$367.83 respectively. Easton has the lowest average per capita total tax bill at \$348.16. (See Table 7 and Graph 5.)

Table 7
TOTAL TAXES PER CAPITA
 2003 - 2007 Actual, 2008 Budget

Year	TOTAL TAXES PER CAPITA				
	Bethlehem	Easton	Lancaster	Reading	York
2003	\$330.22	\$191.37	\$337.37	\$260.70	\$353.84
2004	334.38	250.85	331.09	301.56	390.03
2005	366.41	329.51	383.63	391.92	432.05
2006	414.73	341.36	395.77	413.83	473.66
2007	428.47	360.60	430.34	424.43	491.32
2008 Budget	444.30	395.18	433.27	414.58	510.17
Average	\$386.42	\$348.16	\$385.24	\$367.83	\$441.85
Change 2003 to 2008 Budget					
\$	\$114.08	\$288.47	\$95.90	\$153.88	\$156.34
%	34.5%	150.7%	28.4%	59.0%	44.2%

Graph 5
AVERAGE TOTAL TAXES PER CAPITA
 2003-2007 Actual, 2008 Budget

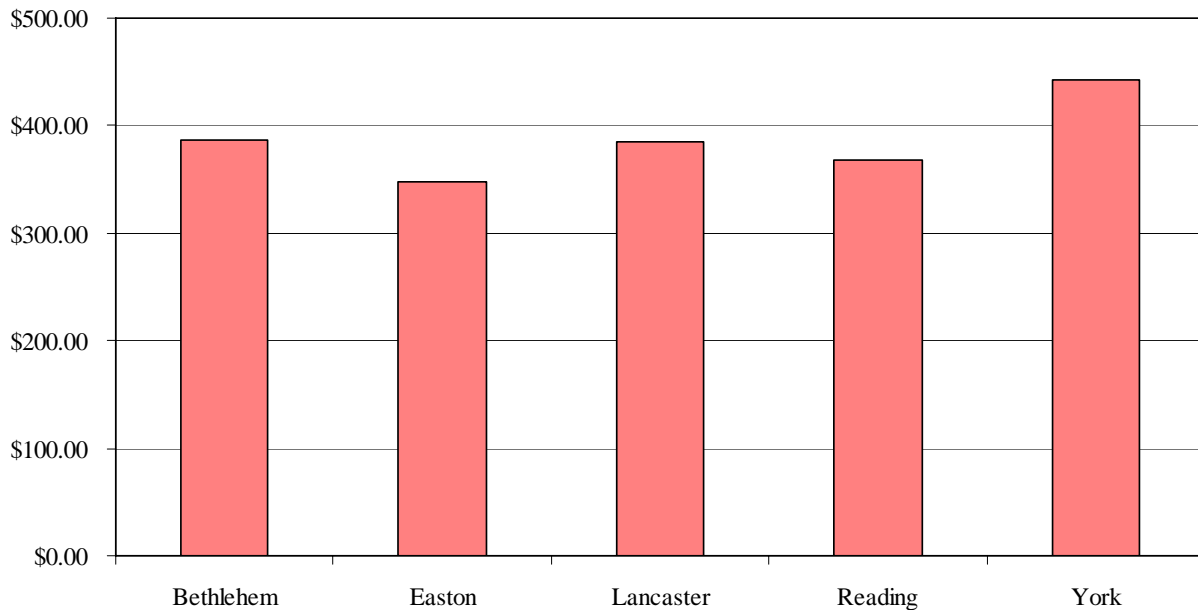


Table 8 and Graph 6 separate total taxes into real estate and non-real estate tax components. The City of Reading has a nearly equal proportion of real estate tax and Act 511 (non-real estate tax) largely because of its higher rate of EIT and Real Estate Transfer Tax under its Home Rule Charter. York has a higher proportion of revenue for non-real estate tax (67.9 percent); Bethlehem has a ratio of real estate to non-real estate taxes of 63.4 percent to 36.6 percent. Easton (72.1 percent to 27.9 percent) and Lancaster (72.2 percent to 27.8 percent) depend more on real estate taxes within their total tax levy. In Reading, the real estate transfer tax at five percent may inhibit or hinder the marketability of real property and perhaps act as a depressant on real property values in the city. The level of this tax represents a substantial cost to the seller (or to the buyer if the closing costs are shifted to the buyer), and extracts a significant portion of equity from a real estate sale. Further increases to the Real Estate Transfer Tax may prove counterproductive to the City’s real estate market.

Table 8
 AVERAGE REAL ESTATE
COMPARED TO NON-REAL ESTATE TAXES PER CAPITA
 2003 - 2007 Actual, 2008 Budget

	Real Estate Taxes		Non-Real Estate Taxes	
	\$	%	\$	%
Bethlehem	245.13	63.4	141.29	36.6
Easton	219.02	72.1	84.64	27.9
Lancaster	278.06	72.2	107.18	27.8
Reading	185.68	50.5	182.16	49.5
York	141.75	32.1	300.10	67.9

Graph 6
AVERAGE PER CAPITA
REAL ESTATE TAXES AND NON REAL ESTATE TAXES
 2003- 2007 Actual, 2008 Budget



Table 9 presents the changes in total taxes during the review period for each municipality. On average, taxes have increased by 6.9 percent for Bethlehem, 30.1 percent for Easton, 5.7 percent for Lancaster, 11.8 percent for Reading and 8.8 percent for York when compared to the 2003 base.

Table 9
CHANGE IN TOTAL TAXES PER CAPITA
 2003 – 2007 Actual, 2008 Budget

	CHANGE FROM PREVIOUS YEAR									
	Bethlehem		Easton		Lancaster		Reading		York	
	\$	%	\$	%	\$	%	\$	%	\$	%
2003-04	4.16	1.3	59.48	31.1	-6.28	-1.9	40.86	15.7	36.20	10.2
2004-05	32.02	9.6	78.66	31.4	52.54	15.9	90.36	30.0	42.01	10.8
2005-06	48.32	13.2	64.74	19.6	12.14	3.2	21.91	5.6	41.61	9.6
2006-07	13.74	3.3	48.86	12.4	34.57	8.7	10.60	2.6	17.66	3.7
2007-08	15.83	3.7	36.73	8.3	2.93	0.7	-9.85	-2.3	18.86	3.8
Avg. Yearly Change	22.82	-	57.69	-	19.18	-	30.78	-	31.27	-
Avg. Change vs. 2003 Base	-	6.9	-	30.1	-	5.7	-	11.8	-	8.8

Police and Fire Expenditures

Throughout this study individual municipal comparisons have been made to police and fire expenditures not only because those expenditures represent the most fundamental of municipal services but are usually the largest expenditure items within the municipal budget. (Due to data restrictions as a result of a change in accounting systems, Easton City’s expenditure data represents an average of four years data, not the six year average of the other municipalities studied.)

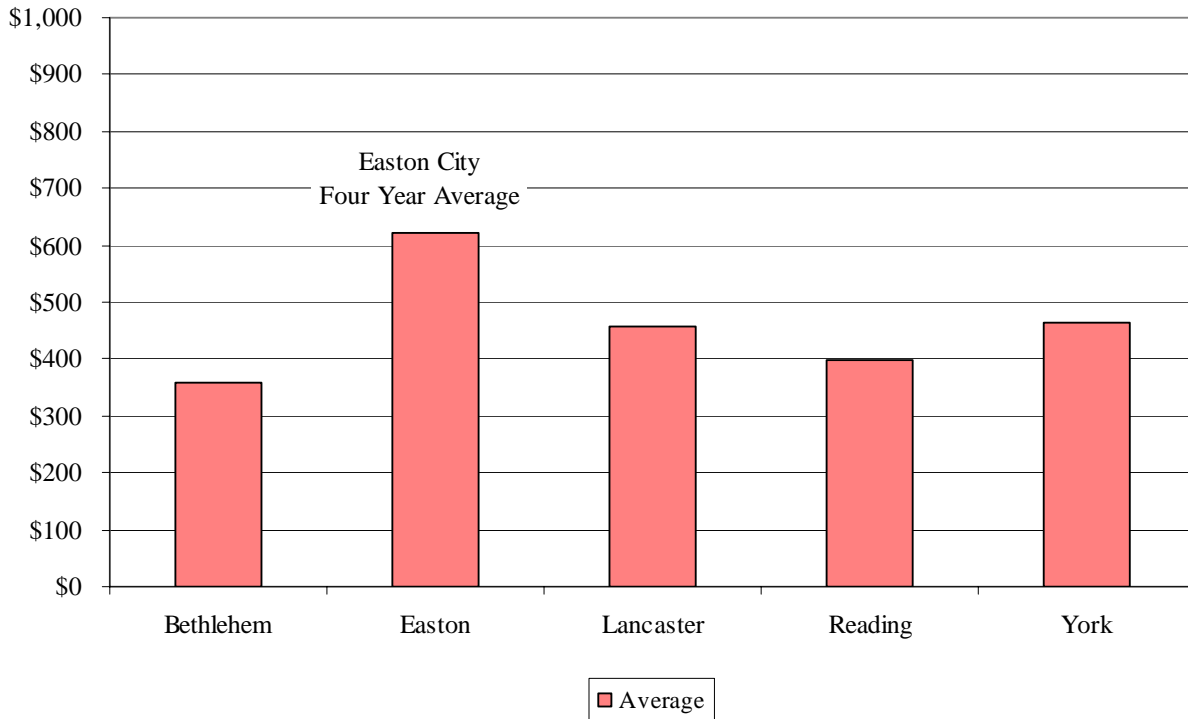
Table 10 and Graph 7 present average police and fire expenditures per capita for each municipality over the period. The average for a six-year period of per capita expenditures for police and fire services range from \$358.59 in Bethlehem to \$463.77 in York. Lancaster has a per capita police and fire expense average of \$458.24, and Reading has \$399.04. Easton’s average per capita expenditures are based upon a four-year period (2005 through 2008) and were \$621.96.

Table 10
POLICE AND FIRE EXPENDITURES PER CAPITA
 2003 - 2007 Actual, 2008 Budget

Year	POLICE AND FIRE EXPENDITURES PER CAPITA				
	Bethlehem ^{1/}	Easton	Lancaster	Reading	York
2003	\$297.46	NA	\$375.63	\$325.48	\$373.14
2004	294.63	NA	382.79	358.80	398.55
2005	327.48	525.42	435.18	395.01	418.02
2006	369.35	616.42	492.91	428.21	508.74
2007	418.44	655.27	517.83	424.98	535.88
2008 Budget	444.20	690.75	545.12	461.78	548.32
Average	\$358.59	\$621.96	\$458.24	\$399.04	\$463.77
Change 2003 to 2008 Budget					
\$	\$146.74	\$165.33	\$169.49	\$136.30	\$175.18
%	49.3%	31.5%	45.1%	41.9%	46.9%

^{1/} Includes EMS

Graph 7
AVERAGE TOTAL POLICE AND FIRE EXPENDITURES PER CAPITA
 Average 2003-2007 Actual, 2008 Budget



In each of the review cities, (except for Bethlehem between 2003 and 2004 and Reading between 2006 and 2007) there has been a yearly increase in the per capita cost of providing police and fire service. (See Table 11.)

Table 11
CHANGE IN POLICE AND FIRE PER CAPITA
 2003 – 2007 Actual, 2008 Budget

	CHANGE FROM PREVIOUS YEAR									
	Bethlehem		Easton		Lancaster		Reading		York	
	\$	%	\$	%	\$	%	\$	%	\$	%
2003-04	-2.83	-1.0	-	-	7.15	1.9	33.32	10.2	25.41	6.8
2004-05	32.85	11.2	-	-	52.39	13.7	36.21	10.1	19.47	4.9
2005-06	41.87	12.8	91.00	17.3	57.73	13.3	33.21	8.4	90.71	21.7
2006-07	49.09	13.3	38.85	6.3	24.91	5.1	-3.23	-0.8	27.14	5.3
2007-08	25.76	6.2	35.48	5.4	27.30	5.3	36.80	8.7	12.43	2.3
				-						
Avg. Yearly Change	29.35	-	55.11	-	33.90	-	27.26	-	35.04	-
Avg. % Change vs. 2003 Base	-	9.9	-	10.5	-	9.0	-	8.4	-	9.4

Real Estate Taxes/Police and Fire Expenditures

Table 12 and Graph 8 provide a comparison of the average per capita real estate taxes to average per capita police expenditures for each municipality. In each case per capita real estate taxes (revenue) are less than per capita police and fire expenditures.

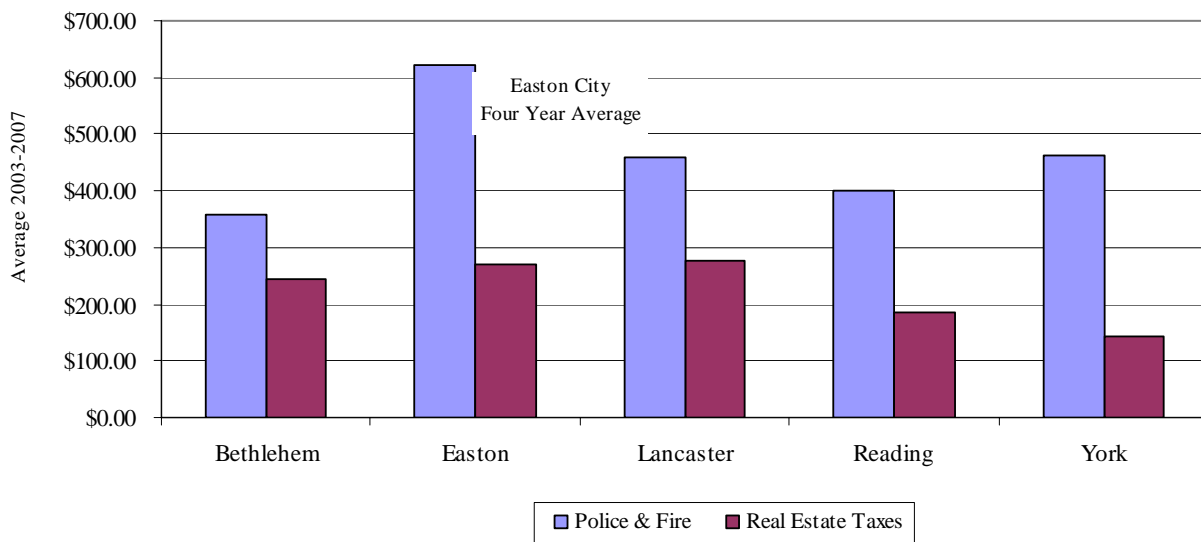
Table 12
PER CAPITA REAL ESTATE TAXES COMPARED TO
POLICE AND FIRE EXPENDITURES
 2003 - 2007 Actual, 2008 Budget

	Real Estate Taxes	Police and Fire	Difference	R.E. Taxes as a % of Police and Fire Expenditures
Bethlehem	\$245.13	\$358.59	(\$113.46)	68.4%
Easton ^{1/}	271.16	621.96	(350.80)	43.6
Lancaster	278.06	458.24	(180.19)	60.7
Reading	185.68	399.04	(213.36)	46.5
York	141.75	463.77	(322.02)	30.6

^{1/} Easton City four-year average.

The difference between real estate taxes per capita and police and fire expenditures per capita ranged from Bethlehem (\$113.46 expenditures over revenues) to Easton (\$350.80 expenditures over revenues). The largest proportion of police and fire expenditures to real estate taxes was in Bethlehem at 68.4 percent, the smallest proportion was in York (30.6 percent). Reading was 46.5 percent; Easton City was 35.2 percent.

Graph 8
REAL ESTATE TAXES COMPARED TO
POLICE AND FIRE EXPENDITURES
 Average 2003-2007



Total Taxes Per Capita Compared to Police and Fire Expenditures Per Capita

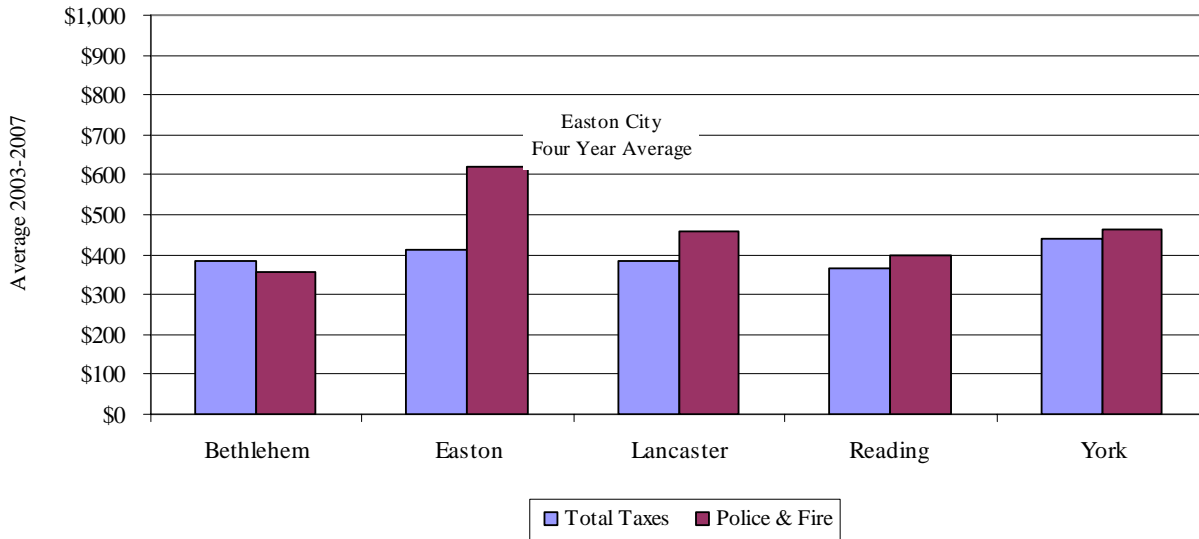
Table 13 and Graph 9 present a comparison of total tax per capita to police and fire expenditures per capita. In Easton, Lancaster, Reading, and York expenditures for police and fire exceed total taxes per capita. However, in Bethlehem total taxes per capita are greater than police and fire expenditures per capita.

Table 13
TOTAL TAXES COMPARED TO POLICE AND FIRE EXPENDITURES
 Average Change Per Capita
 2003 - 2007 Actual, 2008 Budget

	PER CAPITA			Total Taxes as % of Police and Fire Expenditures
	Total Taxes	Police and Fire	Difference	
Bethlehem	\$386.42	\$358.59	\$27.83	107.8%
Easton ^{1/}	411.68	621.96	(210.28)	66.2
Lancaster	385.24	458.24	(73.00)	84.1
Reading	367.83	399.04	(31.21)	92.2
York	441.85	463.77	(21.93)	95.3

^{1/} Easton four-year average for taxes and expenditures.

Graph 9
TOTAL TAXES COMPARED TO
 POLICE AND FIRE EXPENDITURES
 Average 2003-2007



Countywide Comparisons

In an effort to place the prior analysis in a countywide comparative context, PEL compared each of the case study municipalities to the balance of their respective county municipalities. Specifically, PEL compared (on a per capita basis) real estate taxes, total taxes, police expenditures and fire expenditures for each case study municipality to the balance of its

county. For consistency of comparison across municipalities, PEL used 2005 DCED published data.

Real Estate Taxes Per Capita

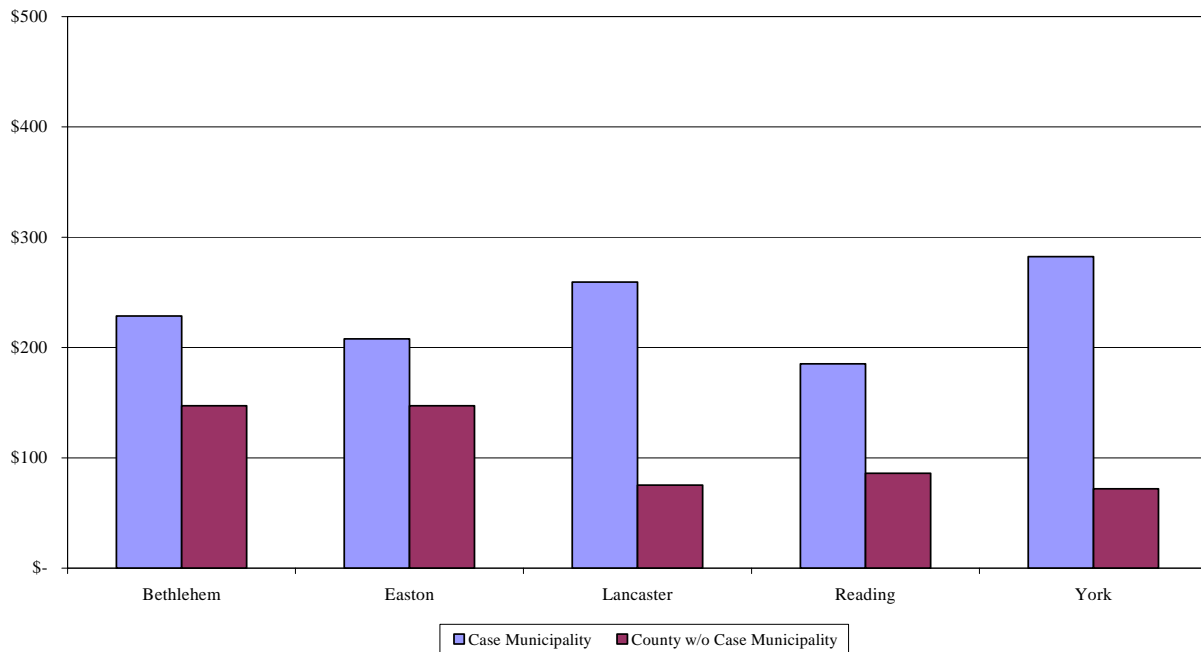
In each case study the per capita real estate tax was greater for the case study city than for the balance of the county, ranging from a low in Easton (1.4 times higher) to a high of 3.9 times as great in York. (See Table 14 and Graph 10.)

Table 14
REAL ESTATE TAXES
 Case Study Municipality vs. County Municipalities without Review Municipality
 2005

<u>Municipality</u>	<u>County</u>	<u>Case Municipality</u>	<u>County w/o Case Municipality</u>	<u>Ratio</u>
Bethlehem	Northampton	\$228.52	\$147.21	1.6
Easton	Northampton	207.84	147.21	1.4
Lancaster	Lancaster	259.25	75.25	3.5
Reading	Berks	185.26	86.07	2.2
York	York	282.36	71.93	3.9

Note: Northampton County excludes Bethlehem and Easton.

Graph 10
PER CAPITA REAL ESTATE TAXES
 Case Municipalities Compared to Balance of County
 2005



Total Taxes Per Capita

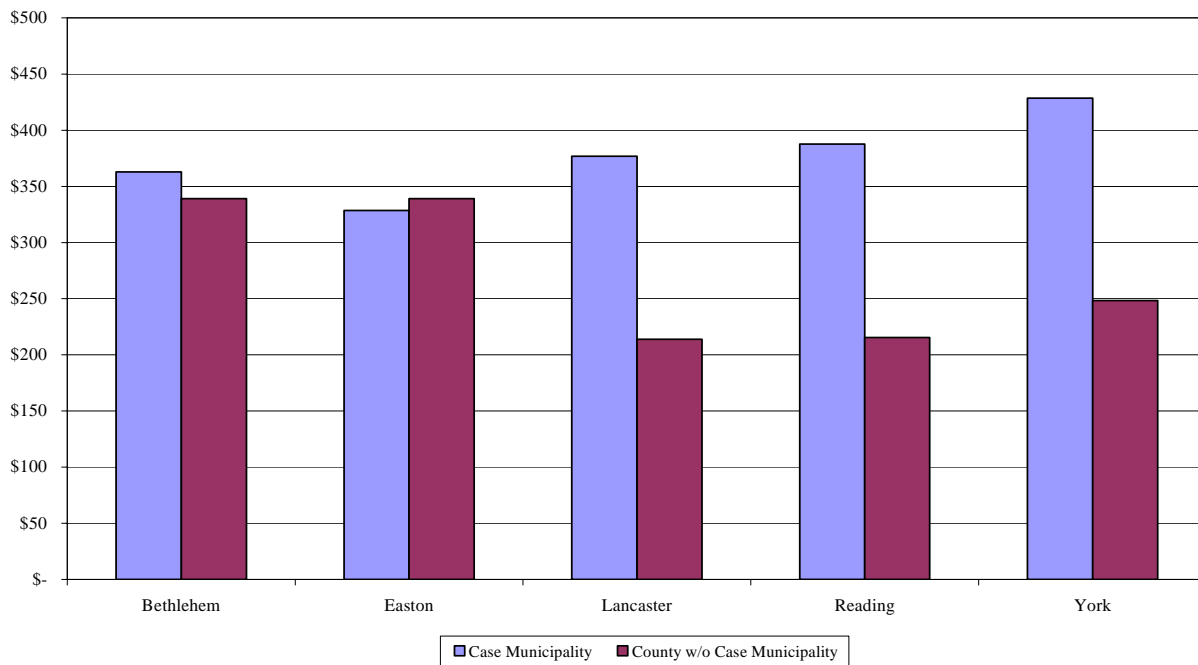
Comparing total taxes per capita, the case study municipalities (except for Easton) have a higher level of taxation than the county municipalities but the overall difference is not as great as it is for real estate taxes alone. The lowest ratios were Bethlehem (1.17) and Easton, (0.97) and the highest ratio is Reading at 1.80. For example, in 2005 (on a per capita basis) Easton residents paid 97 percent in total taxes of what the balance of Northampton County municipalities paid in total taxes. Conversely, Lancaster, Reading, and York per capita total taxes were more than 1.7 times higher than their county municipalities, or for every dollar in total taxes per capita paid in county municipalities, city residents paid over \$1.70. (See Table 15 and Graph 11.)

Table 15
TOTAL TAXES
Study Municipality Compared to County Municipalities without Study Municipality
2005

<u>Municipality</u>	<u>County</u>	<u>Case Municipality</u>	<u>County w/o Case Municipality</u>	<u>Ratio</u>
Bethlehem	Northampton	\$362.85	\$339.13	1.17
Easton	Northampton	328.45	339.13	0.97
Lancaster	Lancaster	376.89	213.90	1.76
Reading	Berks	387.69	215.35	1.80
York	York	428.58	248.33	1.73

Note: Northampton County excludes Bethlehem and Easton.

Graph 11
PER CAPITA TOTAL TAXES
Case Municipalities Compared to Balance of County
2005



The difference in total taxes paid per capita between county municipalities and the reviewed municipalities is smaller largely due to the influence of the Earned Income Tax (EIT). Generally speaking the EIT collected in the balance of the county is higher than in the case study municipalities because of generally higher individual earnings outside the case municipalities. Finally, as described in its profile, Easton has recently become a home rule municipality with the

specific goal of raising its EIT rate beyond the Act 511 limit of 0.5 percent in order to provide additional tax revenue.

Police Expenditures Per Capita

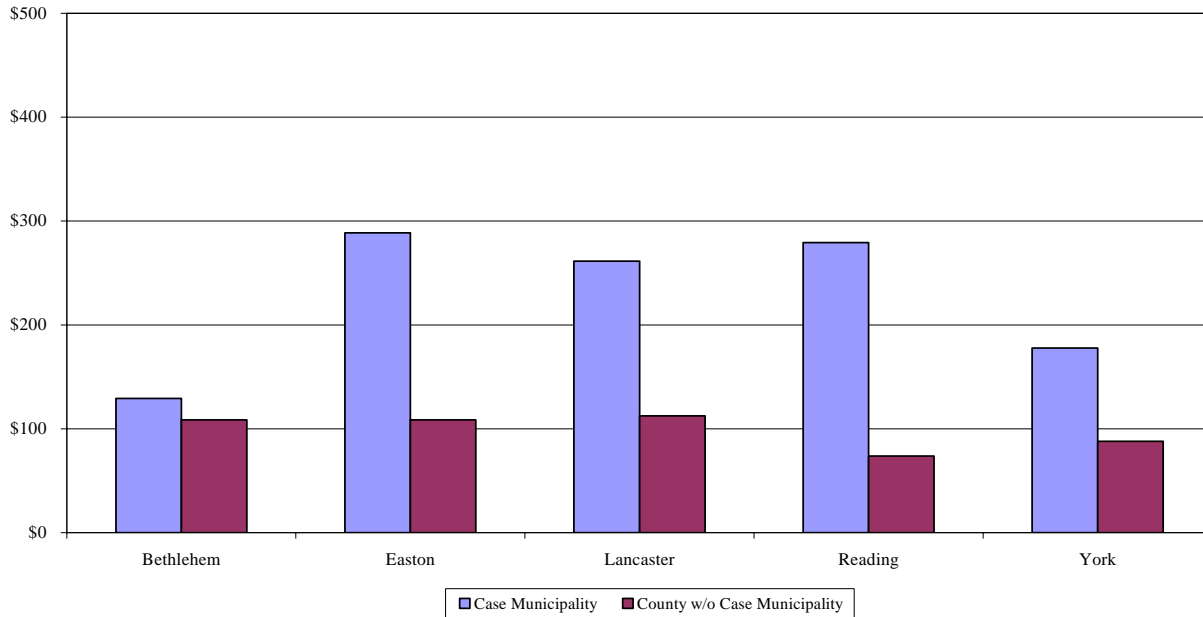
In each instance, the case study municipalities spent more on police operations per capita than did the balance of the county. Bethlehem recorded the lowest rate, 1.19 times more than the county balance and Reading spent the highest rate—3.78 times the balance of the county on a per capita basis. Easton, Lancaster, and York had ratios more than double the per capita police expenditures of the other county municipalities. (See Table 16 and Graph 12.)

Table 16
POLICE EXPENDITURES
 Study Municipality Compared to County without Municipality
 2005

<u>Municipality</u>	<u>County</u>	<u>Case Municipality</u>	<u>County w/o Case Municipality</u>	<u>Ratio</u>
Bethlehem	Northampton	\$129.32	\$108.49	1.19
Easton	Northampton	288.65	108.49	2.66
Lancaster	Lancaster	261.32	112.47	2.32
Reading	Berks	279.22	73.77	3.78
York	York	177.84	87.79	2.03

Note: Northampton County excludes Bethlehem and Easton.

Graph 12
PERCAPITA POLICE EXPENDITURES
 Case Municipalities Compared to Balance of County
 2005



Fire Expenditures Per Capita

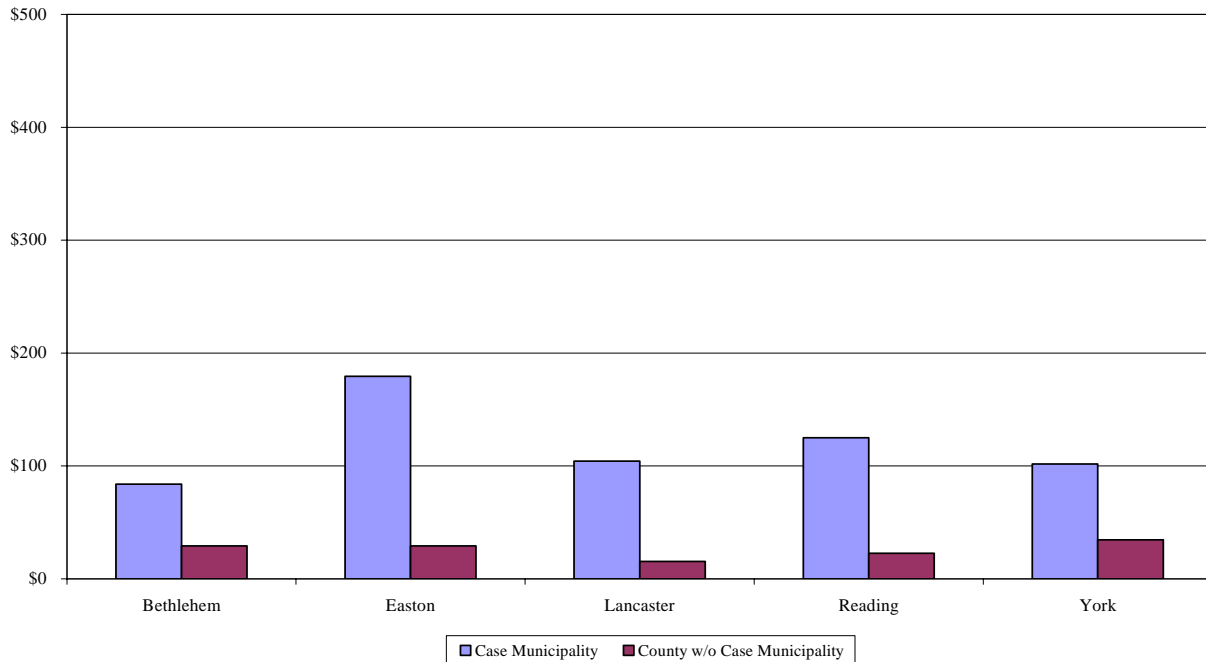
Fire expenditures per capita are shown in Table 17 and Graph 13. Here the case study per capita expenditures are significantly greater than for the balance of the county. For example Bethlehem (the lowest ratio of case municipalities) spent 2.86 times the rest of Northampton County and Lancaster (the highest ratio) spent 6.70 times the balance of their county.

Table 17
FIRE EXPENDITURES
 Study Municipality vs. County without Municipality
 2005

Municipality	County	Case Municipality	County w/o Case Municipality	Ratio
Bethlehem	Northampton	\$ 83.86	\$29.29	2.86
Easton	Northampton	179.51	29.29	6.13
Lancaster	Lancaster	104.14	15.54	6.70
Reading	Berks	124.89	22.66	5.51
York	York	101.72	34.41	2.96

Note: Northampton County excludes Bethlehem and Easton.

Graph 13
PERCAPITA FIRE EXPENDITURES
 Case Municipalities Compared to Balance of County
 2005



The use of fire expenditures as a valid measure can be faulted as a direct service to service comparison of fire expenditures since many of the non-case study county municipalities do not have a paid fire department or have a volunteer department supported at a lower level of expenditures than full-time. However, most mayors of the case study municipalities contend that because of the very nature of their municipality they have no choice but to provide fire service and to meet the corresponding cost.

The primary differences that require fire expenditures:

- The demographic, structural density and building age and usage in the municipality require a fully staffed professional fire service.
- Even without the public safety necessity, existing state law and related court decisions would make it very difficult to terminate an existing fire protection operation.
- In many cases, a public referendum is necessary to disband a paid department.
- Existing volunteer systems in other municipalities are having difficulty in providing manpower for 24-7 coverage that is regularly provided by most paid departments.

Operational Supplements

Operational Supplements

The individual municipal profiles examined the role played by operational supplements in providing additional revenues to meet each municipality’s expenditures.

Table 18 presents operational supplements on a per capita basis for each of the municipalities. Overall the cities of Easton (based on a four-year average) and Reading (over the six year period) had the highest supplements per capita during the review period, although all the municipalities have used them to meet their expenditure requirements. The data indicates that there is a high variability in terms of the dollar value of the supplements on a yearly basis as well as in the categories of each supplement. Graph 14 provides the average per capita operational supplement by municipality.

Table 18
OPERATIONAL SUPPLEMENTS PER CAPITA
 2003 -2007 Actual, 2008 Budget

Year	OPERATIONAL SUPPLEMENTS PER CAPITA				
	Bethlehem	Easton ^{1/}	Lancaster	Reading	York
2003	\$24.17	NA	\$31.27	\$123.15	\$30.71
2004	24.21	NA	67.98	116.94	30.73
2005	24.14	302.45	32.99	158.80	24.66
2006	27.30	292.44	49.87	248.05	42.92
2007	64.20	282.64	51.11	88.76	44.40
2008 Budget	122.66	257.82	72.06	182.87	43.16
Average	\$47.78	\$283.84	\$50.88	\$153.10	\$36.10
Change 2003 to 2008 Budget					
\$	98.49	-44.63	40.79	59.72	12.46
%	407.6%	-14.8%	130.5%	48.5%	40.6%

^{1/} Easton City four-year average.

Graph 14
AVERAGE OPERATIONAL SUPPLEMENT PER CAPITA
 2003-2007 Actual, 2008 Budget

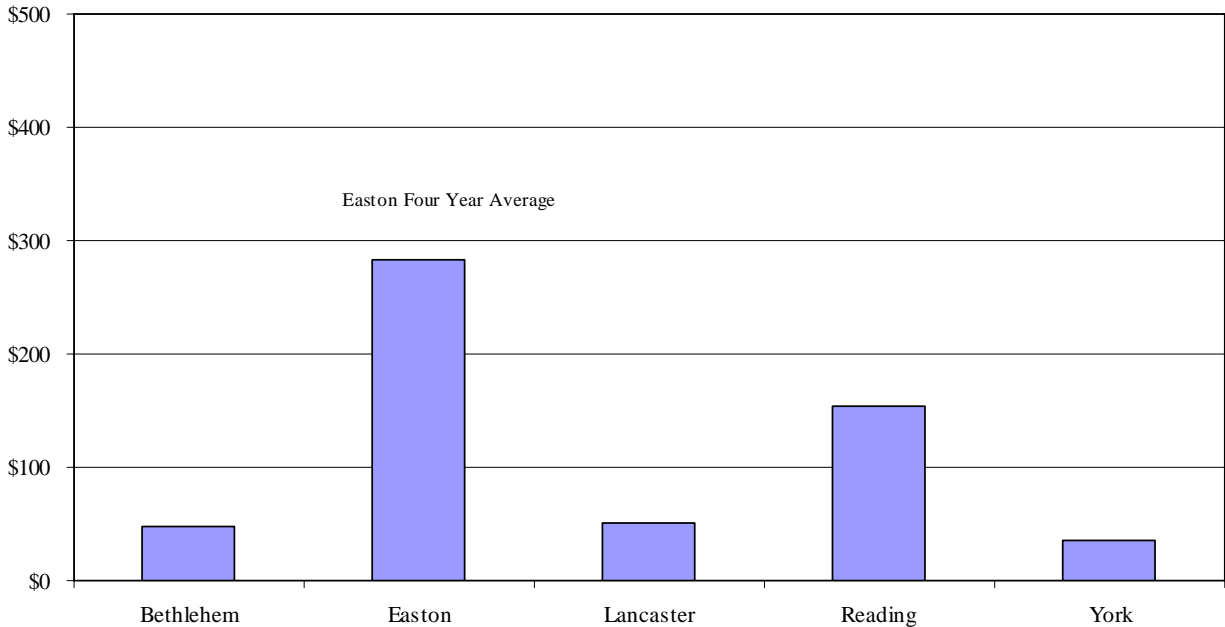
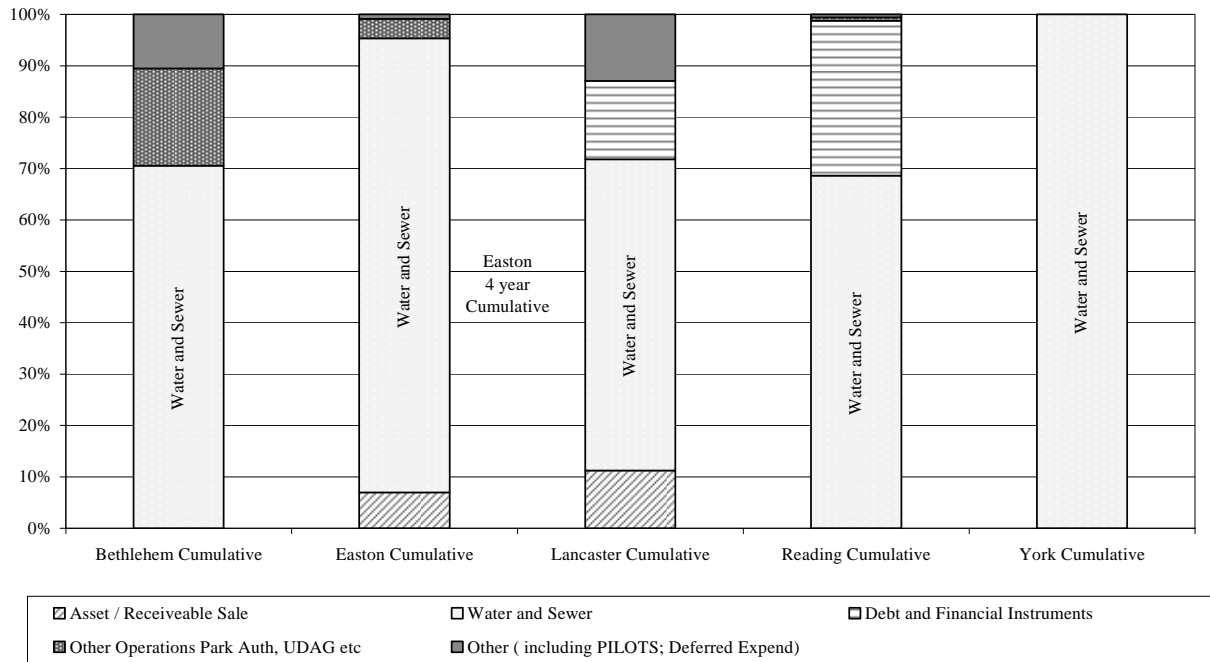


Table 19 and Graph 15 present a listing of the sources of the cumulative supplemental funds for each municipality. Various forms of water/sewer transfers, tapping fees, and the sale of treatment capacity are the principal source of supplemental funds, accounting for between 61 and 71 percent of the total. (It is worth noting that the sale of sewer capacity by Lancaster occurred prior to the review period and therefore is not included. However, that sale makes up most of Lancaster’s current General Fund balance.) With respect to debt and other financial instruments, 30 percent of Reading’s supplements come from this source and 15 percent for Lancaster. PEL included for Lancaster the very large increase in PILOTS which the city received starting in 2006 and thereafter. Other categories make up the remaining percentage including the deferral of medical insurance expenditures in Bethlehem.

Table 19
CUMULATIVE OPERATIONAL SUPPLEMENTS BY MUNICIPALITY
 2003 -2007 Actual, 2008 Budget

	CUMULATIVE OPERATIONAL SUPPLEMENTS									
	Bethlehem	% of Total	Easton	% of Total	Lancaster	% of Total	Reading	% of Total	York	% of Total
Sales of Assets or Receivables	\$ -	-	\$ 2,071,315	7.0	\$ 1,899,184	11.2	\$ -	-	\$ -	-
Water and Sewer	14,546,495	70.5	26,259,190	88.3	10,271,327	60.6	51,039,925	68.6	8,781,000	100.0
Other Operations Sources	3,907,832	-	-	-	-	15.2	500,000	30.1	-	-
Debt and Financial Instruments	-	19.0	1,130,758	3.8	2,579,822	-	22,428,710	0.7	-	-
Other Sources	2,166,667	10.5	260,518	0.9	2,195,064	13.0	424,701	0.6	-	-
Total	\$20,620,994	100.0	\$29,721,781	100.0	\$16,945,397	100.0	\$74,393,336	100.0	\$8,781,000	100.0

Graph 15
CUMULATIVE OPERATIONAL SUPPLEMENTS
 2003 - 2007 Actual, 2008 Budget



Effect of Operational Supplements on Historical Budgets

The importance of the increased used of operational supplements is based on the need— in any given budget period—to “plug” or make up a potential revenue shortfall in order to bring a revenue budget into balance with expenditures.

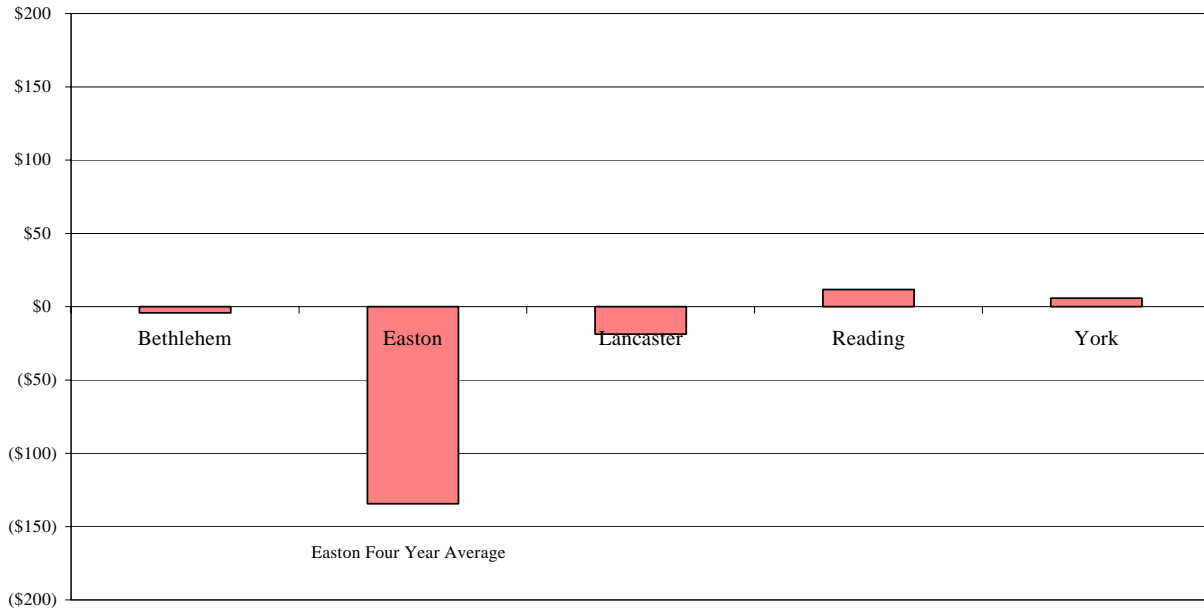
Table 20 provides the reported per capita surplus or deficits for each municipality. For most years each municipality was in a deficit position with the following exceptions: Reading showed a surplus in 2005 and 2006, and balanced in 2008, by using operational supplements,

other finance options, and by resorting to extraordinary actions such as the sale of a city-owned lake. The use of these fiscal devices throughout the review period thus does not properly depict Reading’s fiscal condition. Lancaster demonstrated a surplus in 2004; and Bethlehem had a small surplus in 2003, 2004, and projected 2008. (See Graph 16.)

Table 20
SURPLUS/(DEFICIT) PER CAPITA WITH OPERATIONAL SUPPLEMENTS
 2003 -2007 Actual, 2008 Budget

Year	SURPLUS/(DEFICIT) PER CAPITA				
	Bethlehem	Easton	Lancaster	Reading	York
2003	\$1.84	NA	(\$33.32)	(\$43.82)	\$ 6.26
2004	6.72	NA	28.26	(25.01)	26.70
2005	(3.60)	(114.28)	(16.98)	75.68	22.60
2006	(27.74)	(123.48)	(25.29)	118.09	(7.70)
2007	(4.01)	(125.90)	(18.76)	(54.02)	(13.43)
2008Budget	1.85	(173.70)	(46.49)	0	0.48
Average	(\$5.67)	(\$134.34)	(\$18.76)	\$11.82	\$5.82

Graph 16
AVERAGE SURPLUS (DEFICIT) PER CAPITA
Bethlehem, Easton, Lancaster, Reading, York
 2003-2007 Actual, 2008 Budget

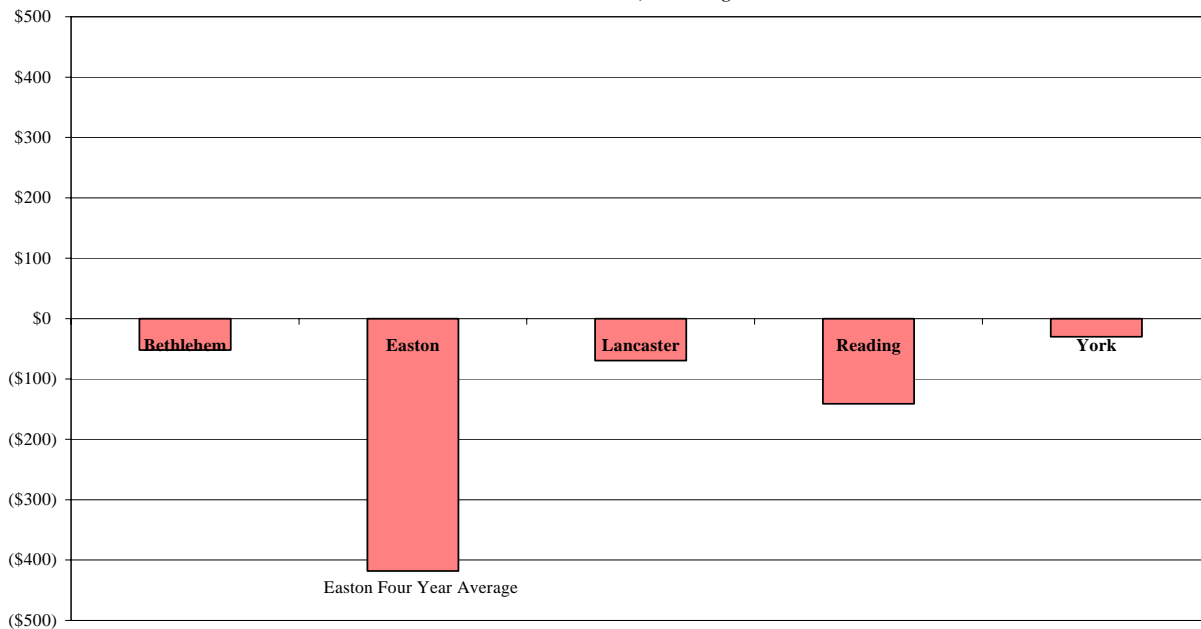


However, when the operational supplements are removed from the municipal surplus calculations, the financial results are altered; deficits would have occurred for each year in every municipality if there had been no use of operational supplements. Further the deficits per capita would have been quite large and for the most part larger in the most recent years. For the 2008 budget year Reading would go from “breakeven” to a \$183 per person deficit; Bethlehem from a \$1.85 per capita surplus to a \$120.81 deficit and Lancaster from \$46.49 deficit per capita to a \$118.55 deficit per capita, York would have a \$0.48 surplus per capita to a \$42.69 per capita deficit. (See Tables 20 and 21 and Graph 17.)

Table 21
SURPLUS/(DEFICIT) PER CAPITA WITHOUT OPERATIONAL SUPPLEMENTS
 2003 -2007 Actual, 2008 Budget

Year	SURPLUS/(DEFICIT) PER CAPITA				
	Bethlehem	Easton	Lancaster	Reading	York
2003	(\$22.33)	NA	(\$64.59)	(\$166.97)	(\$24.44)
2004	(17.49)	NA	(39.72)	(141.95)	(4.03)
2005	(27.73)	(416.73)	(49.97)	(83.13)	(2.06)
2006	(55.05)	(415.92)	(75.15)	(129.96)	(50.62)
2007	(68.21)	(408.54)	(69.86)	(142.78)	(57.83)
2008 Budget	(120.81)	(431.52)	(118.55)	(182.87)	(42.69)
Average	(\$51.94)	(\$418.18)	(\$69.64)	(\$141.28)	(\$30.28)

Graph 17
AVERAGE SURPLUS (DEFICIT) PER CAPITA
WITHOUT OPERATIONAL SUPPLEMENTS
2003-2007 Actual, 2008 Budget



Perhaps more surprising is that for the review period (including 2008 budget figures) Reading would go from an average surplus of nearly \$12 per capita with supplements to a deficit of \$141 per person; Bethlehem from a \$6 per capita deficit to \$52 deficit without supplements; Lancaster an average deficit of \$19 per person with supplements to \$70 per capita deficit.

In all cases, operational supplements are controversial but are of critical importance in maintaining the fiscal balances of the case study municipalities. The public policy concern is whether these levels of supplemental revenue are expected to be used to sustain the increasing municipal cost structure. Of more immediate concern is the frequent use of debt as a supplement. Debt that is created today to fill a current budget gap will exacerbate the municipality’s future fiscal balance by removing future revenue that must be used to satisfy the recurring cost of debt.

CHAPTER 9

CASE STUDY OBSERVATIONS

Bethlehem, Easton, Lancaster, Reading and York Cities

The five cities examined in this review are all third class cities, with populations ranging from slightly over 26,000 to just in excess of 80,000. All have suffered from historical population stagnation or declines, although some have recently shown early signs of some rebound in population. The five cities have also seen their tax bases, both as property values and as earned income, stagnate or decline as well. As a generalization, it is not inaccurate to say that the cities are older, smaller, and poorer than they were over the past several decades.

Nonetheless, the five cities remain the economic, social, political, and religious hubs of their particular regions. The cities still provide the focus of economic activity for their regions, and also provide the locus for the educational, governmental, religious, and healthcare institutions that serve both the cities and the surrounding areas. **Therefore, the cities are obligated to provide the level of public safety and infrastructure services that maintains the integrity of the city and the vitality of the region.**

The case studies illustrate the central issue facing the cities, to continue to provide an expected level of public safety and infrastructure services from a declining tax base which is increasingly unable to support these services. **The cities' total revenue streams consist of taxes, non-tax revenues such as fees and charges for services, and a variety of sources of income that range from one time elements such as debt and derivatives or sale of assets to annual recurring subsidies from utility operations.**

Each city depends on the revenue collected primarily from real estate and Act 511 taxes, particularly the Earned Income Tax. For the cities in these case studies, the real estate tax has become an essentially static revenue source. Property assessments, the basis for real estate taxation, have been slow to grow and reflect the limited ability of the cities to achieve significant property appreciation through new development. There is typically little room for new development on vacant land in these cities, for example, the most significant property development in these studies is being built upon the site of a bankrupt steel mill. Politically, the cities must compete with the school districts and the counties for the real estate tax base, and as such cannot significantly compound the increased tax millage on the assessment base. For the

Act 511 taxes, the cities must also share these revenue sources with their school districts. Of the available taxes, the earned income tax (EIT), local services tax (LST), and the real estate transfer tax are the most productive levies.

The EIT has performed with lagging growth in the case study cities, with most cities showing only minimal annual growth in this tax source. Reflecting the demographic changes of the cities, the EIT—levied in Pennsylvania based on place of residence—generates a tax level that is representative of the cities' residents' prosperity, not the overall level of earnings from the people who work within the cities. The LST tax, levied on employees based upon the location of work, does generate significant revenue for the cities, but is limited to the maximum range of \$47 to \$52 per employee per year. The disparity between place of work and place of residence is reflected in the collection totals in some of the cities as the LST revenues approach 60 to 70 percent or more of EIT revenues. Even the home rule cities of Reading and Easton, with the ability to raise the EIT rate above the statutory maximum, do so as a replacement or substitute for increases in the real estate tax, as well as a response to the stagnant earnings base of their residents.

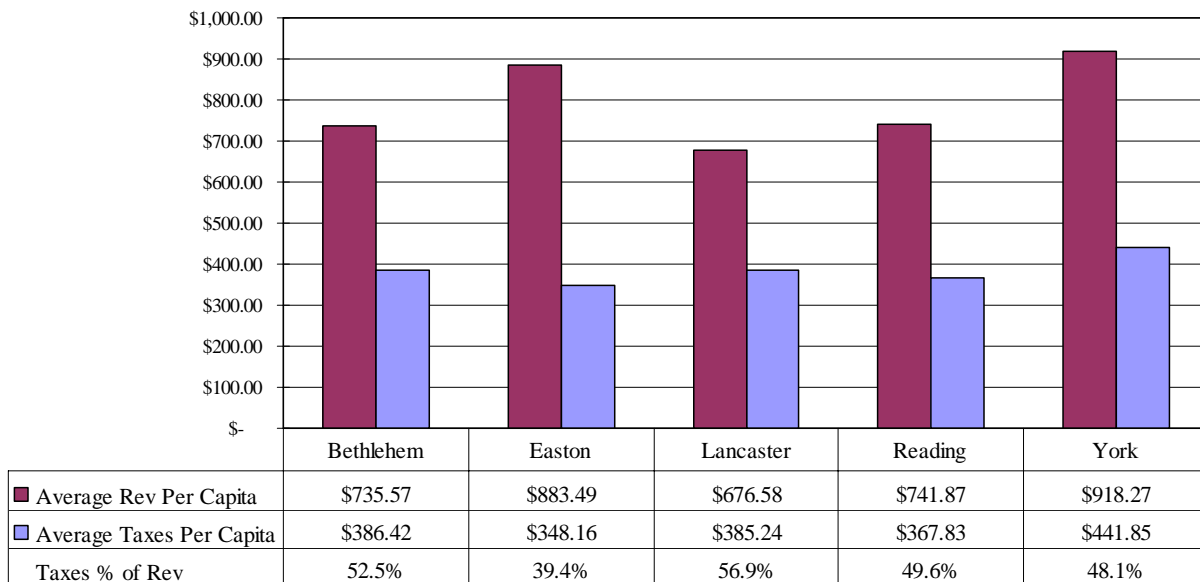
PEL analyzed the cities' ability to pay for the basic elements of municipal services solely from the taxes collected in the cities. Public safety, specifically the provision of police and fire services, was selected as the indispensable service provided by the cities. **In all but one of the case study cities, total taxes collected each year were insufficient to pay for police and fire services. In other words, all the taxes levied within the city do not generate sufficient revenue to pay for public safety, let alone the other basic functions of the government such as general administration, public works, and debt service. No city in any of the case studies could support public safety, general administration, public works and debt service from their existing tax base.**

All of the cities have had to look to other non-tax sources of revenue to provide the resources to pay for government operations. Fees and charges for services are used by all cities to supplement the tax base and cover everything from copies of police reports to charges for water and sewer services. The cities' abilities to generate revenues from fees and charges for services are limited only by state statute or the cities' inability to creatively generate income from other sources. Even with the cities' ability to generate non-tax revenue such as debt from derivatives or sales of assets, the case studies demonstrate these revenues, combined with total

taxes collected, are still not sufficient to reliably fund ongoing operations on an annual basis. **This report did not examine the public policy question of using debt to be repaid from successive year budgets—debt used to pay for current year operations; this financial technique is a paramount public policy issue that must be addressed by the Commonwealth.**

Based upon the case study data, tax revenue as a percentage of total revenue is not always the main source of revenue for the municipality. While it can be assumed that tax revenue would be the largest portion of the municipal revenue source, that assumption is not always true. Indeed, based on per capita measures, taxes as a percent of total revenue ranges from a low of 34.4 percent to a high of 56.9 percent. Municipalities in the case studies are forced to pay for expenditures from sources that are not generally considered tax revenue, but from fees for services (often services once paid for by taxes) and for transfers of revenues created from fees for services of a specific type, such as water and sewer or parking. (See Graph 1.)

Graph 1
PER CAPITA AVERAGE TOTAL TAXES VS. AVERAGE TOTAL REVENUE
 Bethlehem, Easton, Lancaster, Reading, York
 2003 - 2007



Each of the cities has had to resort to what PEL has termed “operational supplements” to generate enough income each year to fund ongoing city operations. Taxes and non-tax revenues simply do not and cannot support the expected level of services that the cities provide on an

annual basis. These operational supplements can take many forms. In all the case study cities, operational supplements in the form of subsidy payments are collected by the cities' general funds from enterprise funds, primarily the water and sewer funds. These utility operations are structured to generate revenue to provide a fiscal resource each year and to pay for the cost of providing the service. Other operational supplements include: sale of assets; drawdown of fund balances; use of proceeds from debt issues, including refinancing or restructuring of outstanding debt; use of derivative products such as swaps or swaptions to generate up front current year payments; and other creative and risky techniques.

These cities have relied increasingly on these operational supplements to fill the financing gap that exists each year between the revenues generated and the expenditures required to support the provided level of services. Each city uses operational supplements, and has relied on them more each year throughout the review period.

The cities' dilemma is fundamentally a revenue problem. Expenditures, particularly for public safety, infrastructure, general administration, and debt service are determined by the levels of services that the cities are expected, indeed almost required, to provide in their roles as regional leaders and by their populations. Revenue bases, already restricted by statute and by demographics, are further reduced by the amount of tax-exempt property in each city. These properties house the educational, governmental, health care, religious, and other public service institutions that make up the essential fabric of regional life, and also provide a significant amount of employment for the residents of the cities and for the regions. The cities do not have the flexibility to reach beyond their tax bases to capture the revenue generated by the location and employment of the institutions in the same way that counties or school districts are able to achieve through taxing a regional base. Unlike counties or school districts, the cities, must still provide the essential public safety and infrastructure needed to protect and enhance these institutions. If the cities cannot capture the revenue streams produced as a result of their status as regional economic generators, the cities will be compelled to search for even more creative methods to pay for the services that their citizens have a right to expect from their local government tax dollars.