Joint Public Hearing on Act 47
Pennsylvania House of Representatives
Finance, Local Government and Urban Affairs Committees
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Testimony
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Good morning Chairs O'Neill, Wheatley, Harper, Freeman, Keller and O'Brien, and Members of the House Finance, Local Government and Urban Affairs Committees. My name is Phil Klotz, Executive Director of the Local Government Commission. With me today are Dave Greene, Assistant Director-Legal Counsel, and Kris Gazsi, Associate Legal Counsel for the Commission. Thank you for inviting us testify at today's Joint Public Hearing on Act 47. The Local Government Commission is a bipartisan, bicameral agency of the Pennsylvania General Assembly comprised of ten legislators—three from the majority party and two from the minority party in each chamber—collectively working for more effective and efficient local government in Pennsylvania. Our testimony highlights the background, purpose and contents of Act 47.

The Municipalities Financial Recovery Act, or Act 47, was enacted in 1987 as the product of a Local Government Commission-sponsored task force, convened to look for solutions for growing financial problems among municipalities in Pennsylvania. Many municipalities faced, and still struggle with, financial challenges related to changes in the business cycle and shifts in population and economic opportunity, as well as inadequate local management and rising legacy costs, and other cyclical and structural issues.

The 1980s task force found that short-term distress, typically caused by a municipality's inability to balance its budget, can be determined by variables that measure a budgetary balance between revenues and expenditures (surplus or deficit), the average short-term debt as a percentage of total revenues and average debt service costs as a percentage of total revenues. By contrast, long-term distress, also called structural distress, may occur where various factors create a persistent imbalance between the funding available to the municipality and the duties and services that the municipality must or chooses to provide. These factors may include a loss of an external funding source like federal aid, a change in tax base caused by population shifts or an increase in internal costs, including those related to increased service needs. Act 47 was enacted to provide a process for "distressed" municipalities to work with the Department of Community and Economic Development (DCED) and reestablish financial stability.

Under Act 47, DCED may issue a declaration of distress after it finds that a triggering event has occurred, either automatically, as in the case of a bankruptcy filing, or after a party with standing petitions the Department to apply a set of statutory criteria under Chapter 2 of the act to assess the fiscal condition of the municipality.

After a declaration of distress, DCED appoints a coordinator to analyze the financial situation, issue a report on findings, and propose a plan for recovery. The coordinator is given broad authority to inspect records related to the municipality's operations and finances.

The recovery plan, developed under Chapter 2, may recommend changes to the municipality's staffing, assets or services, and may also propose multimunicipal cooperation, privatization, debt restructuring and disposition of assets, among other things. A distressed municipality may be authorized by the plan to petition the court of common pleas for special authorization to increase the real estate tax, the earned income tax on residents and nonresidents, as well as the local services tax, where the court finds that appropriate conditions are met. In addition, an Act 47 municipality may permanently replace its mercantile/business privilege tax with payroll preparation tax. A municipality in recovery also benefits from priority consideration for any economic development grants available through the Commonwealth, and assistance in pursuing labor agreements that fit within the structure of the recovery plan.

An adopted plan must be implemented by the coordinator directly, by another specified person, or with the coordinator's oversight. During the course of plan implementation, the coordinator is also required to participate in the municipality's budget process to ensure that the annual budget is compatible with the plan's provisions.

However, where a municipality fails to adopt or implement a plan proposed by the recovery coordinator or develop an alternative plan with the Secretary of DCED's approval, the Department may suspend certain funding sources to the municipality from the Commonwealth, or recommend more significant action to the Governor.

The Governor may declare a fiscal emergency upon a finding that the municipality has become insolvent and is unwilling or unable to adopt or implement a recovery plan. A fiscal emergency has only been declared once, shortly after the provisions were first adopted into Act 47 in 2011 in response to a period of crisis in Harrisburg when the city's financial situation threatened an imminent possibility of bankruptcy.

In a fiscal emergency, the department must develop an emergency action plan that ensures the maintenance of defined vital and necessary services. Thereafter, the Secretary of DCED may appoint a receiver to implement the emergency action plan and form a more permanent recovery plan subject to court approval. The receiver is required to ensure the implementation of the recovery plan, which includes the power to require the city to implement the plan, provide for the disposition of property, and negotiate intergovernmental cooperation agreements. The receiver may also directly approve, disapprove, modify, reject, terminate or renegotiate contracts and agreements with the distressed municipality, and act on the municipality's behalf in the case of a bankruptcy filing. Once a fiscal emergency has been declared, a city may not petition a court of common pleas for an increase in the rate of earned income taxes on nonresidents.

Following Senate and House joint committee hearings on Act 47 in fall 2011 precipitated by Harrisburg's financial crisis, and recognition that the act proved to be insufficiently effective in putting distressed municipalities back on firm financial footing, the Commission empaneled a task force during the 2013-2014 legislative session, which resulted in Act 199 of 2014, comprehensively revising Act 47 for the first time in over 25 years. Key among the findings of the task force was that the Act 47 program had succeeded in stabilizing distressed municipalities, but largely struggled to move municipalities from stabilization to sustainable recovery. Thus many Act 47 municipalities remained in recovery for decades under state intervention.

Among other things, Act 199 added a formal structure to an existing regulatory early intervention program designed to help municipalities avoid formal intervention under Act 47, established a five-year time period for recovery with an option to adopt a three-year exit plan, diversified tax revenue enhancements available during recovery with court approval, and created an alternative to the recovery process by which a nonviable municipality could voluntarily wind down its affairs. In many respects these amendments sought to ensure that where a municipality could not avoid the Act 47 program all together, it would be required to plot a course with the recovery coordinator to plan for a future where it would need to operate without the special tools available during Act 47 recovery.

This fall, five years have passed since Harrisburg adopted and began the implementation of the recovery plan formed by the receiver. Together with the recovery coordinator, the city is engaged in the choices posed by Act 199 when a municipality considers a three-year exit plan. About half of the 17 distressed communities with Act 47 recovery plans have either adopted exit plans or will consider them during the upcoming year. Since the enactment of Act 199, five municipalities have emerged from Act 47 recovery; all but one of them have done so with home rule charters that support greater tax rate flexibility.

This concludes our testimony. Dave Greene, Kris Gazsi and I will do our best to answer any questions that you may have. Thank you.