Better Know a Budget:

City of Scranton

What does the 2014 Budget Say About Itself?

- The 2014 operating budget is $130.5 million, up from $111 million in 2013

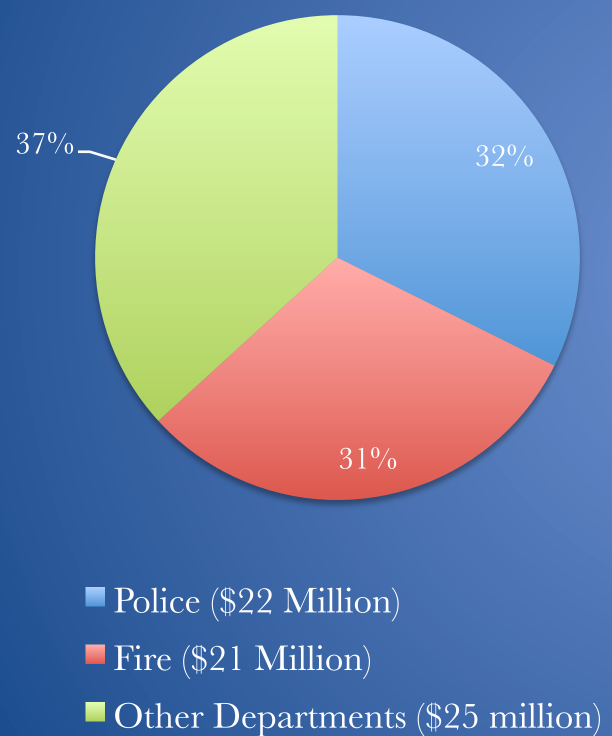
- But only about $68 million is spent on the City's departments:
  - $22 million for the Police Department (17%)
  - $21 million for the Fire Department (17%)
  - $25 million for all non-Public Safety Depts. (e.g., Mayor, Business Admin, Council, Public Works, etc). So that's 19%

- Of this $68 million, less than half is salary ($28 million)

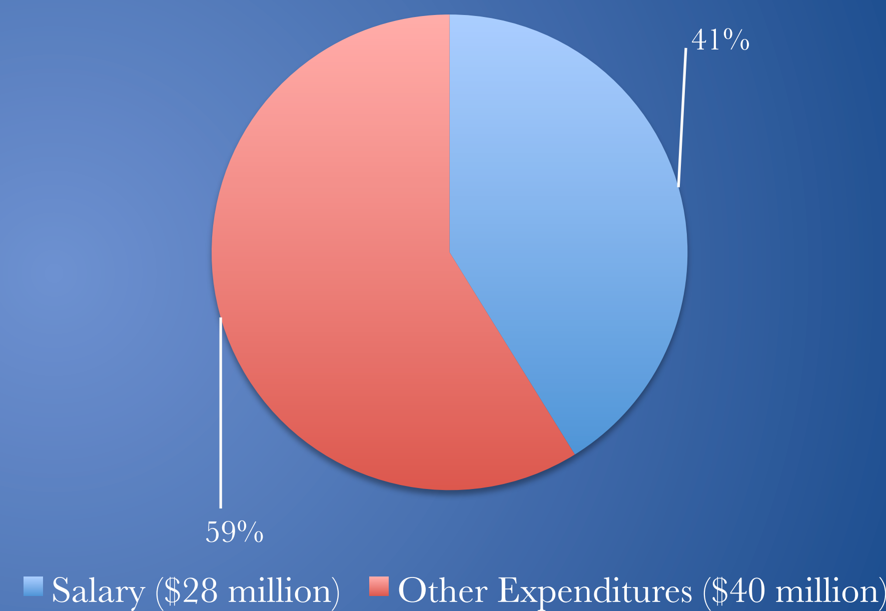
- **In total, this "departmental spend" accounts for 53% of the City's budget.**

What does the 2014 Budget Say About Itself?

City Spending by Department



Salary v. Other Expenditures



What does the 2014 Budget Say About Itself?

- So, that means it costs about $68 million to "run" the City—i.e., pay for most of the *services* that the City does (police and fire protection, garbage collection, parks and recreation, etc).

- But…what about the **$40 million** of the $68 million that's *not* salary?

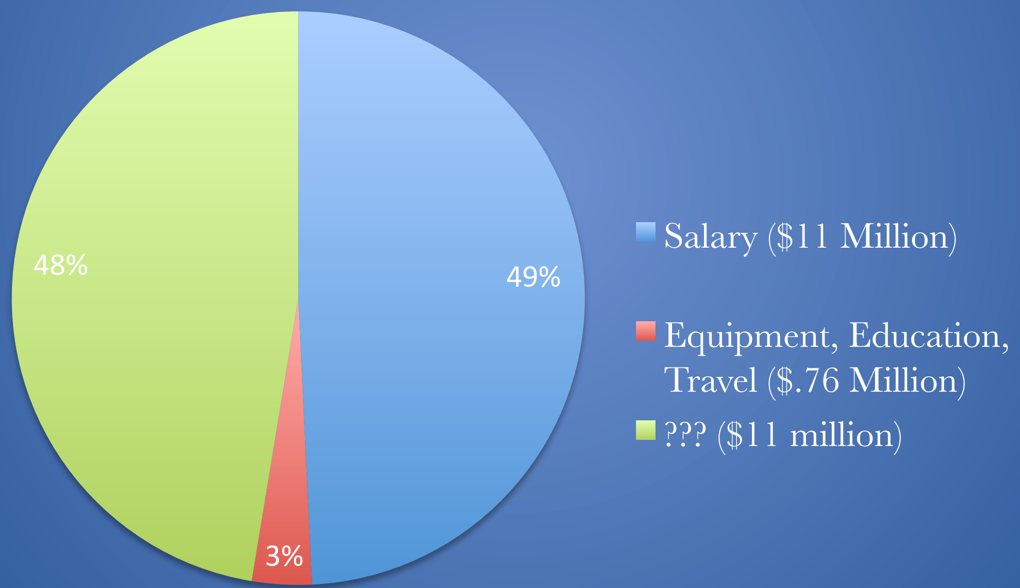
- …and what about the remaining **$60 million** of the $130 million budget?

- **First, let's go through how the $68 million breaks down—we'll look at the $60 million later**

What do our City services *really* cost?

- Let's look at the **Police Department** as an example.

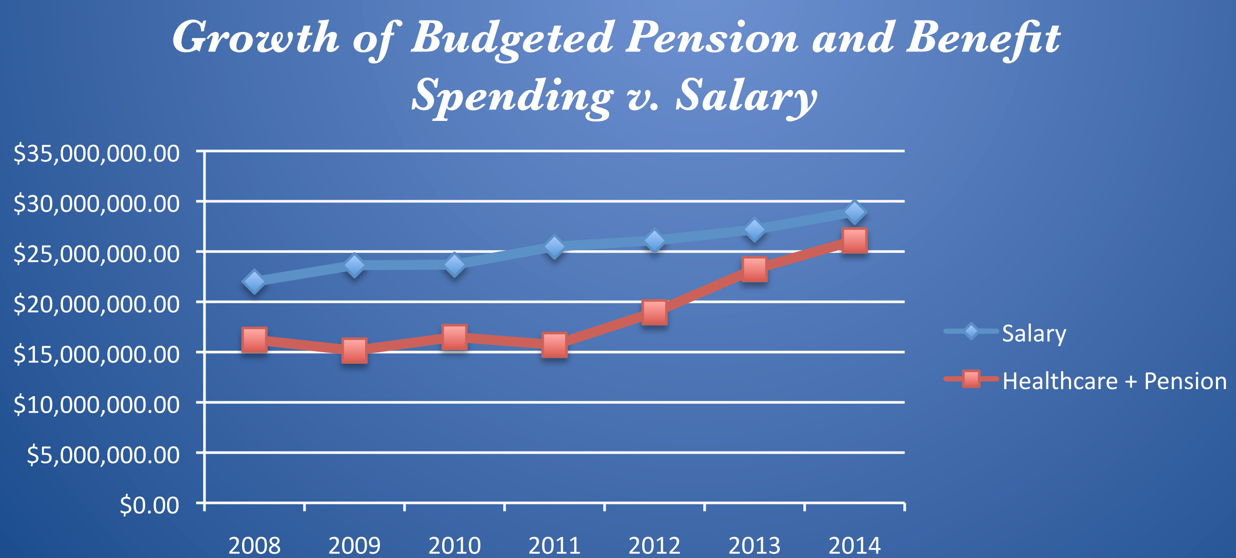
Police Department Expenditure Breakdown



- What accounts for the remaining **48 percent**?

What do our City services *really* cost?

- That remaining 48% in Police Department spending? **It's for pension and benefits (PenBens).** Healthcare is by far the largest component of benefits
- Contracts with the City's unions mandate a salary increase that works out to about 2% annually.
- But the growth in pension and benefit spending is much more steep, growing on an average of 7% annually since 2008 and average of **15%** since 2012. The City is **contractually** obligated to provide PenBens to all eligible employees
- And this trend holds true across the City, with PenBens accounting for a greater and greater share of City spending; it's not unlikely they will surpass salary in the coming years.



2008:
$16 million

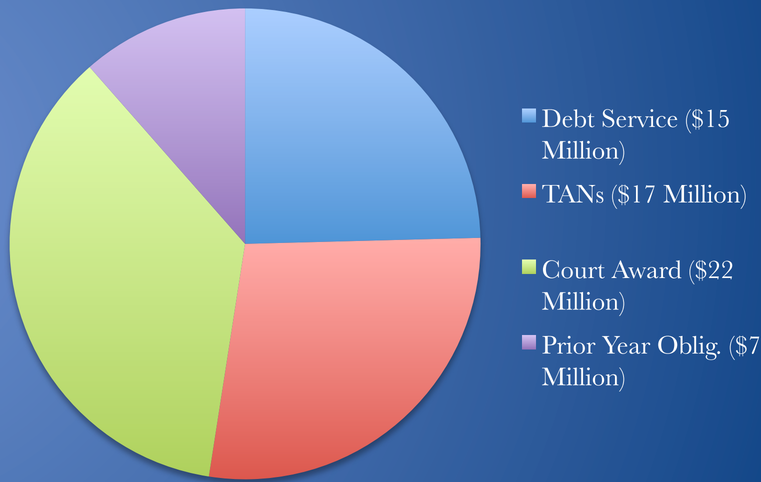
2014:
$25 million

Increase of: 62.5%

What does the 2014 Budget Say About Itself?

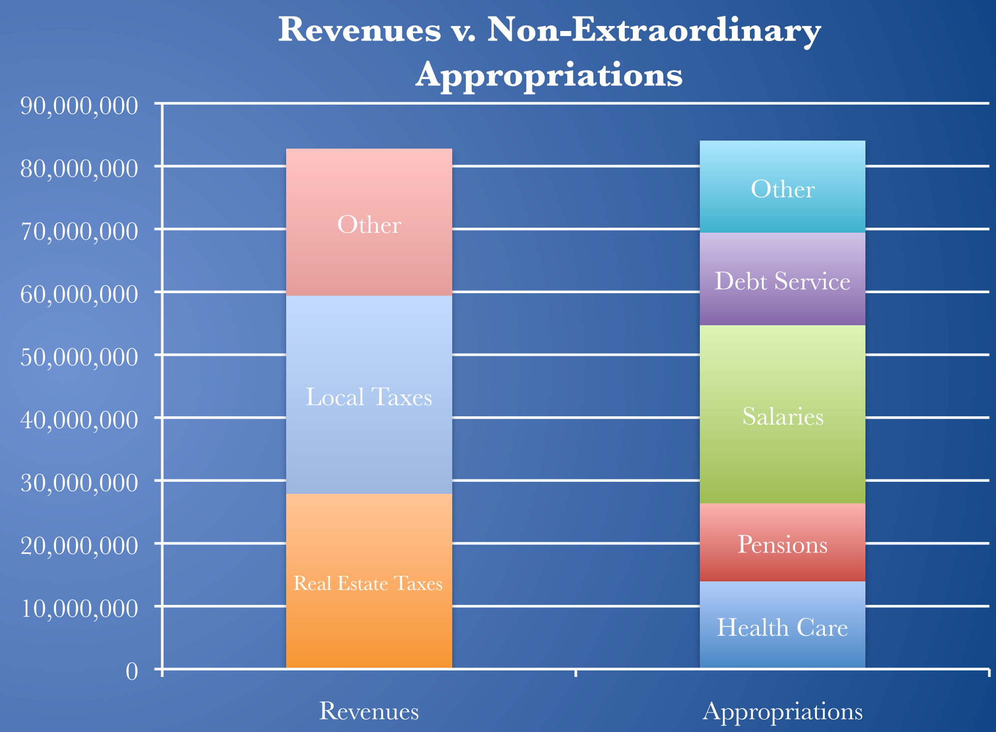
- This left over $60 million is made up of what's known as "Non-Departmental Spending," which includes
  - $15 million for **debt service** *excluding*:
  - $17 million (realized at $12.5 million) for what are called **Tax Anticipation Notes (TANs)**
    - TANs allow the City to get cash to help pay for current operating expenses, which the City pledges to pay back with tax revenues.
    - This is a common approach for cities, given the nature of a city's revenue cycle.
  - $22 million for a one-time court award, which supplies back pay to the Unions
  - $7 million for outstanding prior year obligations
- Several of these costs—particularly the court award—are extraordinary and will require immediate action

Non-Dept. Spending

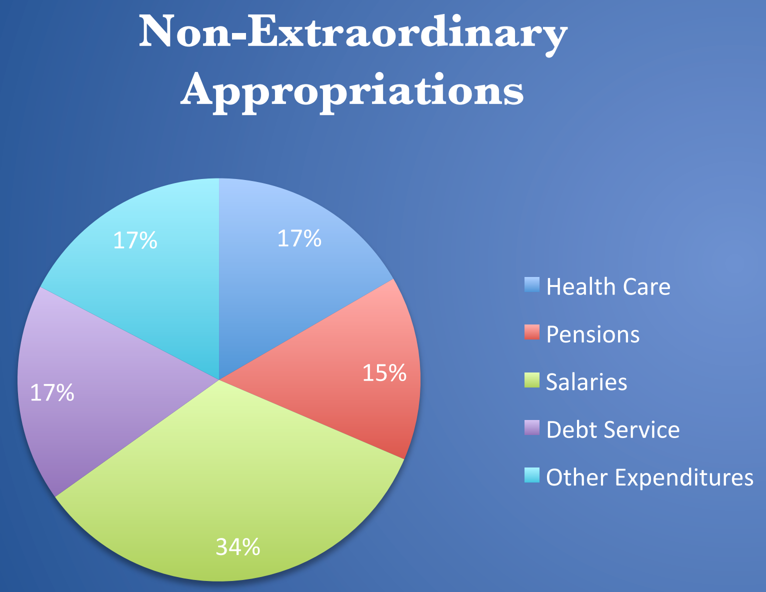


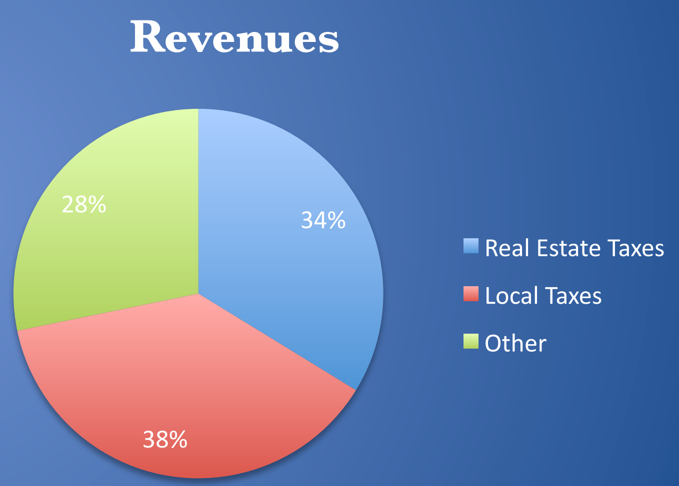
Non-Extraordinary Revenues & Appropriations

- When you take out extraordinary expenses and the TAN, Scranton's really only making an appropriation of **$84 million**
- That's 1/3 less than the operating expenditures listed in 2014 Budget and $1 million *less* than 2012.
- Non-extraordinary revenues are $82 million (taxes, fines, fees, permits, parking meters etc).
- So, in reality, the City's pretty close to being structurally balanced



Non-Extraordinary Revenues & Appropriations



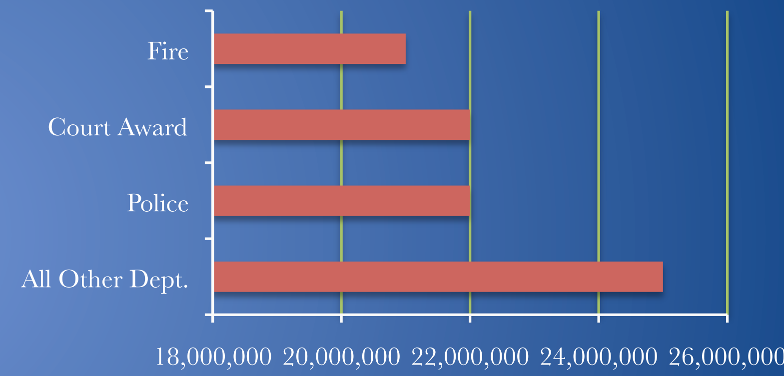


What is "Marbleization" and what does it mean for Scranton?

- Much of Scranton's budget is what we call "marbleized"
  - This refers to expenses that are essentially fixed, usually by a labor contract or the terms of a bond
  - If the City went "out of business," i.e., stopped providing services, real estate taxes would be just enough to be able to pay the City's marbleized costs
- Between marbleized costs and the need to maintain the quality of City services, there is not too much room to maneuver on the expense side of the budget
  - but there are some possibilities, particularly in health care
- **So, we need to look to *revenue*-based solutions**
  - But how do we tackle one of the most immediate problems—paying for the judgment?

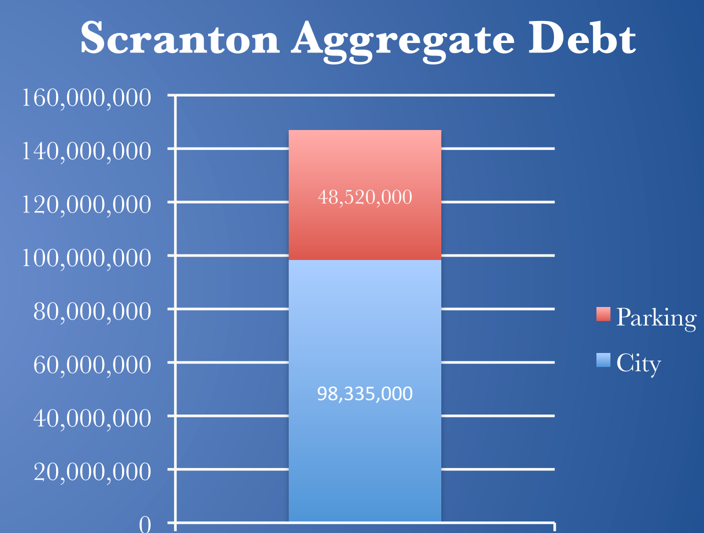
Paying for the Judgment

- The most immediate issue facing the City is the $22 million judgment.
  – How do we pay for it?
- One answer would be to issue bonds, but this poses two problems:
  – Creating the future need for the City to make *even more* debt service payments, adding further strain on City services
  – Can the City even *issue* bonds, given its difficult financial situation?
- What can we do?
  – Bring the cost of the judgment into the City's general debt



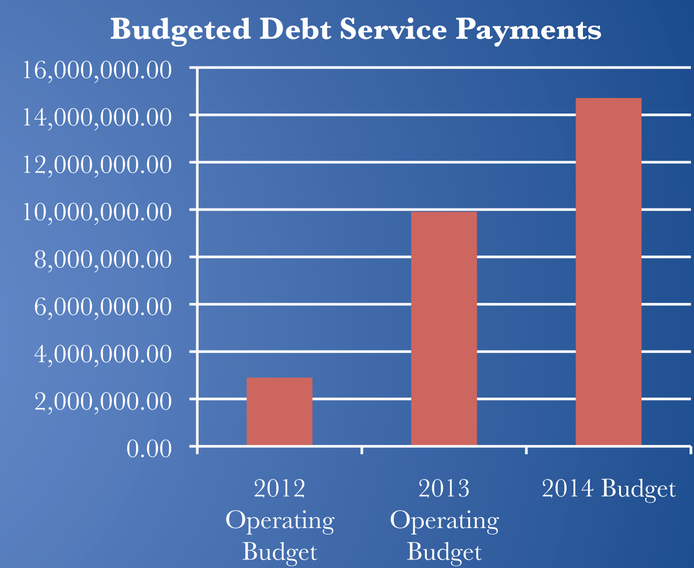
Debt

- Debt may not be pretty, but it is an essential part of running a City
  - We often need it to pay for new roads, buildings, and to serve as a sort of "rainy day" fund.
- But the more debts a City takes on, the harder it is to get money to pay for the things we need
  - Things got even harder when the Scranton Parking Authority defaulted, essentially saddling the City with the bill for all of the *Parking Authority's* outstanding debt
  - About 15% of the City's long term debt payments this year are for the Parking Authority.



The (Recent) History of Scranton's Debt

- While long term debt is traditionally used to pay for capital investments, such as new roads, police cars, and public buildings, it can also be used to pay for operating expenses
  - This is not considered to be a sustainable or sound fiscal practice, and is, accordingly, frowned upon by the credit rating agencies
  - Scranton began to take on debt to cover operating expenses—including other debt service payments—beginning in 2010, causing its credit rating to suffer significantly
  - Today, Scranton does not even have an official credit rating



Outstanding Debt

Domain	Title	Debtor	Year	Principal	Principal + Interest
City	Emmaus General Authority GO	City	2002	5,325,000.00	6,923,800.00
City	GO Series A	City	2003	520,000.00	538,200.00
City	GO Series B	City	2003	28,200,000.00	41,417,477.58
City	GO Series C	City	2003	14,625,000.00	24,570,490.00
City	Federally Taxable GO Series D	City	2003	8,170,000.00	10,773,950.00
City	Guaranteed Lease Revenue Bonds	Sewer	2004	1,615,000.00	1,818,551.84
City	Federally Taxable Guaranteed Lease Revenue Bonds	Redevelopment Authority	2006	9,580,000.00	13,826,385.00
City	Federally Taxable Guaranteed Lease Revenue Bonds	Redevelopment Authority	2008	5,880,000.00	8,577,682.97
City	Series A of 2012 (Unfunded Deficit Financing)	City	2012	9,080,000.00	13,355,075.00
City	Series B of 2012 (Refunding of Nov-Dec 2012 Portion	City	2012	1,355,000.00	1,994,625.00
City	Series C of 2012 (Unfunded Deficit Financing)	City	2012	9,075,000.00	12,568,462.50
City	Series A of 2013 (Refunding of Feb-Dec 2013 Portion	City	2013	4,910,000.00	7,071,950.00
City	**Total - City**	**City**		**98,335,000.00**	**143,436,649.89**
Parking	General Revenue	Parking	2004	14,025,000.00	22,152,735.00
Parking	General Revenue	Parking	2006	3,560,000.00	5,658,610.00
Parking	General Revenue	Parking	2007	30,935,000.00	61,008,618.75
Parking	**Total - Parking**	**Parking**		**48,520,000.00**	**88,819,963.75**
Total	**Grand Total**			**146,855,000.00**	**232,256,613.64**

The Consequences of Bad Credit

- The consequence is that Scranton has difficulty entering the long term debt market at fair rates, so it's hard to make the investments that the City needs.
  - If Scranton were to try to issue bonds, interest rates would likely be high
  - Without a credible and measurable recovery plan restructuring the City's debt will be difficult
- Short term debt—or, TANs—have also become far more expensive. This year's TAN has an effective 9% rate, or about 5 points beyond the average

What's Making Creditors Worried?

- The amount of the City's outstanding debt: $98 Million
  - Especially with the added burden of the Scranton Parking Authority's debt: $48 million
  - **That makes for a total of $146 million in aggregate debt**
- The City's pension and benefit obligations
  - In 2011, $60 million in assets, liabilities of $173 million. **$113** million deficit with a funding ratio of 34. The Commonwealth refers to this as "severely distressed"
- The immediate crisis (the $22 million) judgment

Solutions

- Scranton must find ways to pay for its pension liabilities in a stable and direct way
  - New sources of revenue
    - Local Services Tax
    - Act 205 Tax
  - Revenue Strategies
    - Dedicated Real Estate Tax mils
    - Earmarking directly to fund the pension
  - Scranton's parking assets should be responsibly sold off or completely in-housed to get out from under the Parking Authority's debt burden
    - Dedicated meter, fine, and Parking Tax revenue to help pay down the debt
- The unions *are* part of the solution
  - Good faith negotiations need to begin immediately.

Improving the revenues we already have

- Scranton only collects about 86% of the taxes owed to it annually.
  - It should be 98 percent. How do we get there?
- Fines, fees, permits, licenses, and other City revenues were about **$2 million under budget** in 2013
  - Improvements can no doubt be made here, but do we know if the revenue targets are truly accurate?
  - Should we *really* expect $1 million from parking tickets when we only make $390,000?
  - Take on a revenue cycle officer

What are PILOTs and how do we get them?

- Payments in Lieu of Taxes, or PILOTs, are a negotiated amount that traditionally tax exempt entities in a municipality pay to the city for municipal services

- The City should seek to renegotiate PILOTs with key non-profits, in part by indentifying how PILOT revenue will be spent in ways that directly impact non-profit payers

Healthcare Savings

- There are opportunities to reduce spending on City healthcare benefits without violating the terms of a contract or reducing the quality of care. In fact, the quality of care can go up!
- Wellness programs help bring down the costs of chronic health issues and reduce the number of visits to costly specialists
  - Wellness "stipends" (Aetna offers $75,000)
  - A 2010 study from the *Journal of Health Affairs* found that for every dollar a firm invested in wellness programs, it would save $3.27 on medical costs and $2.73 on absenteeism-related costs.
- What about creating a medical home for City employees?
  - Integrity Health, Toms River, NJ: under 2% growth in health care spend—*negative* growth some years
  - Columbia, SC: $2 million in savings for year one

This is just the beginning.

Thank You