* Report on the Budget and Finances of the City of Scranton

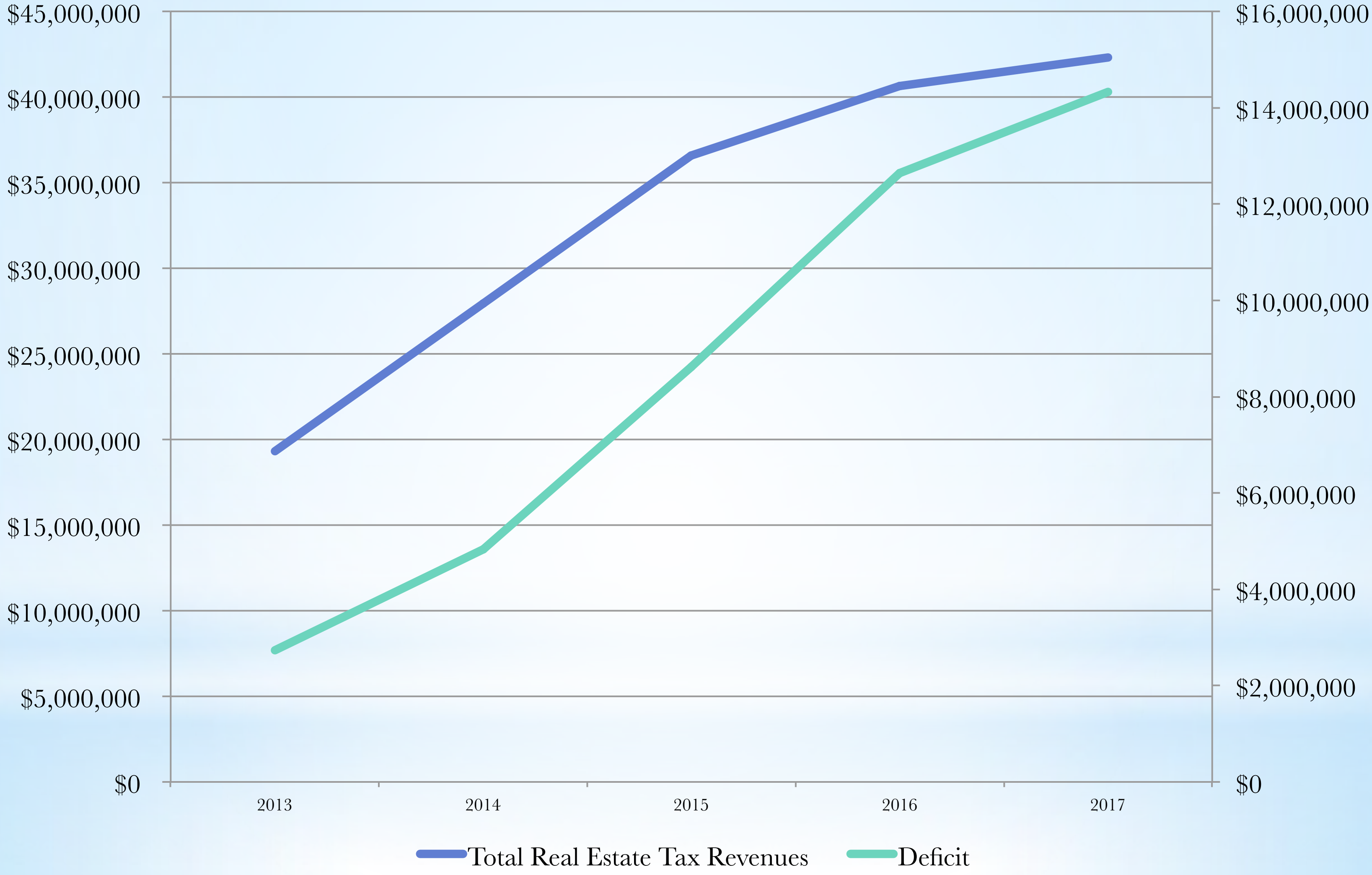
HJA Strategies, LLC.

July 2014

* Should the City fail to act decisively, total Real Estate tax revenues would have to be increased by at least 119 percent over 2013 levels to meet the projected 2017 deficit. This is $23 million in absolute terms
* Or, some portion of this would be made up by a further resident EIT increase
* Cuts to City services would also be inevitable
* The City would remain in Act 47

The Stakes

Total Real Estate Tax Revenues & Deficit Projections (No Expanded Revenue Sources)

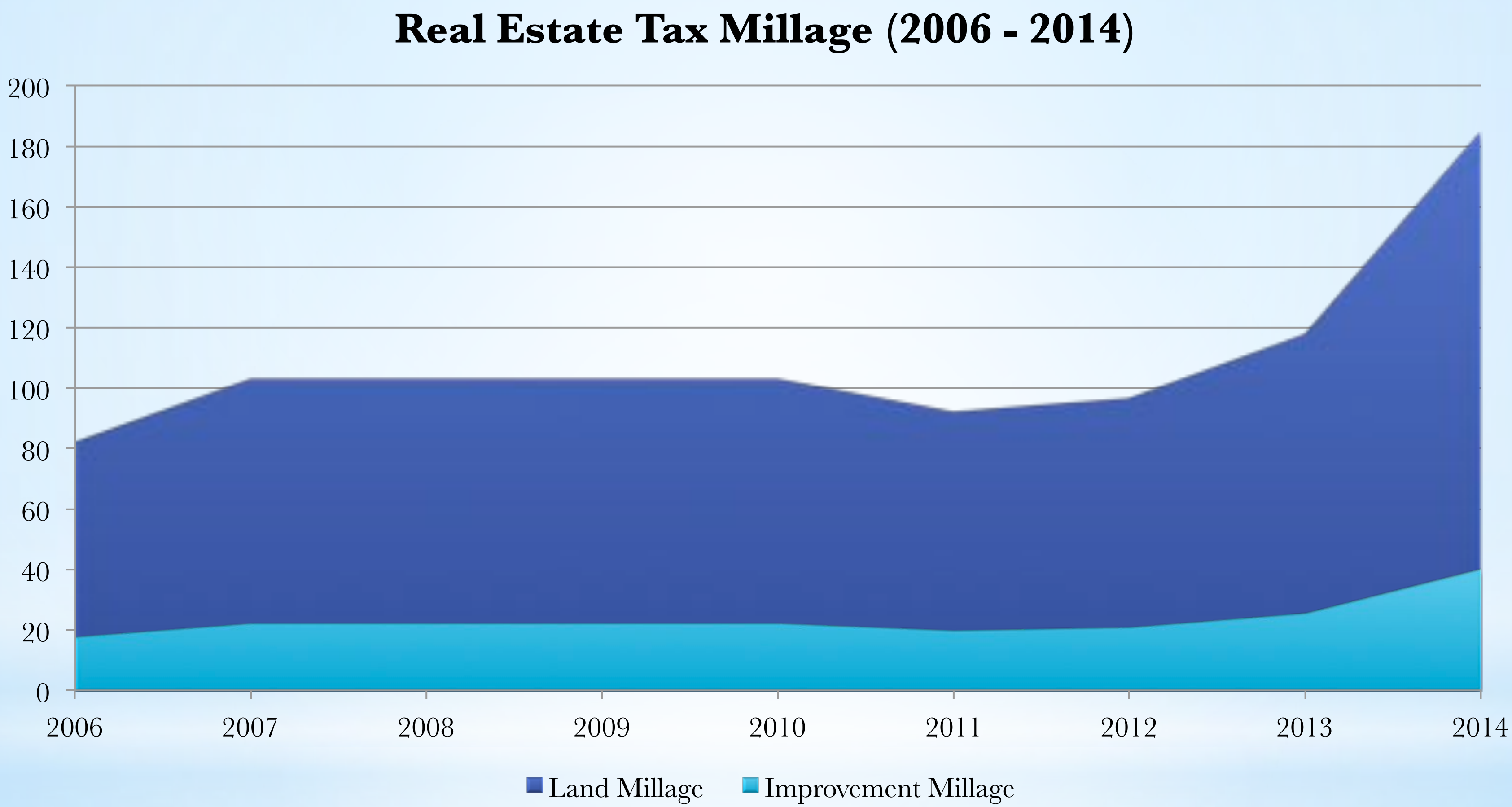


Category	Amt. Change	Total
		$130,195,163.00
Less Direct Compensation	$87,147.00	$130,108,016.00
Less Interest & Debt Excluding Tans	$1,378,881.00	$128,729,135.00
Less TAN Repayment	$4,295,070.00	$124,434,065.00
Less Unpaid Prior Year Pension	$4,000,000.00	$120,434,065.00
Less Court Awards	$22,000,000.00	$98,434,065.00
Add Health Insurance	$1,020,545.00	$99,454,610.00
Add Other Employee Expenses	$45,872.00	**$99,500,482.00**

* Adjusted Appropriations

Category	Amt. Change	Total
		$130,536,998.00
Miscellaneous Revenues	($175,000.00)	$130,361,998.00
Sale of Assets	($1,700,000.00)	$128,661,998.00
Interfund Transfers	($1,987,418.00)	$126,674,580.00
Tax Anticipation Notes	($4,000,000.00)	$122,674,580.00
Bond Issue Proceeds	($28,000,000.00)	**$94,674,580.00**
True Appropriation		**$99,500,482.00**
Adjusted Deficit		**$4,825,902.00**

* Benchmarking: Adjusted Revenues and Deficit



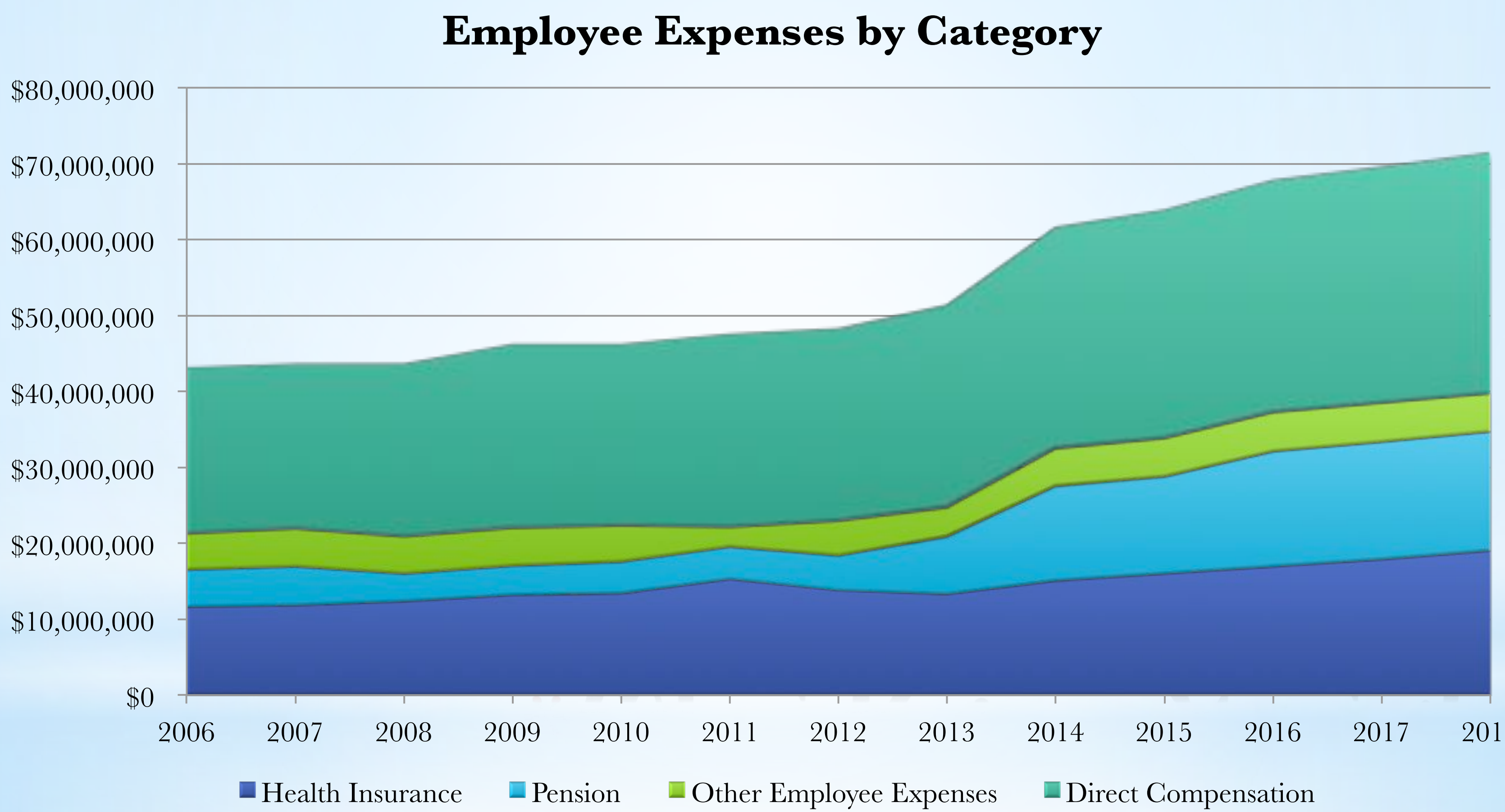
From 2006 to 2014, the City's total Real Estate Tax millage increased by 125 percent

* There has not been a reassessment in Scranton since the late 1960s. The County must approve it and has refused to fully execute
* For every $1 generated in Real Estate Taxes today, Scranton could be getting a $1.35 if there were a reassessment
* Creates an inequitable tax regime and disincentivizes new construction and renovations

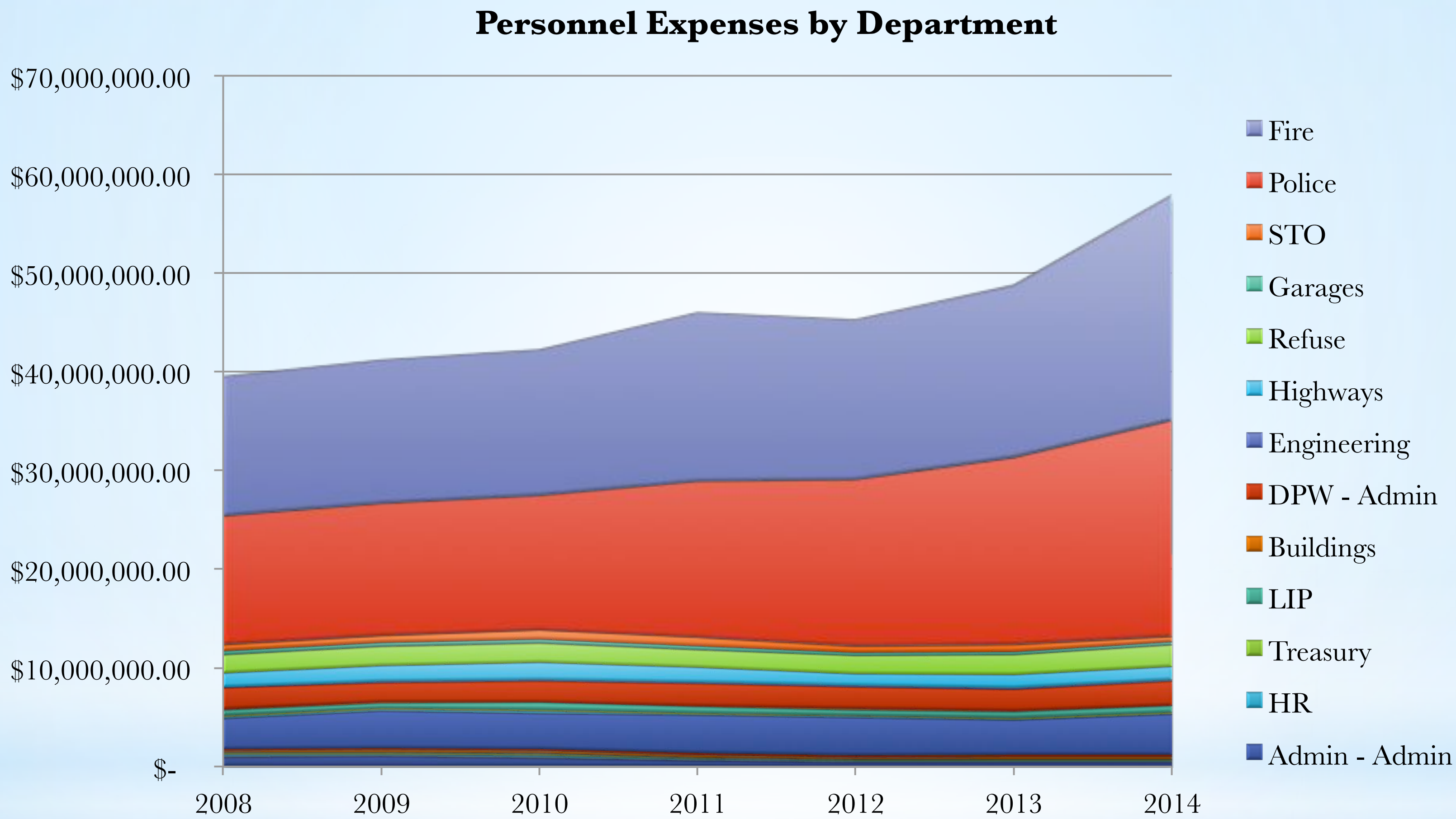
Property Reassessment

* The proportion of the total appropriation constituted by employee expenses is between 60% and 63%
* It is projected to climb somewhat, reaching 66% in 2018
* Employee expenses grew by approximately 44% between 2006 – 2014
* They are projected to grow by 66% between 2006 - 2018.
* The City's Earned Income Tax, the single largest source of revenue until 2014, increased by just 24 percent between 2006 and 2014.

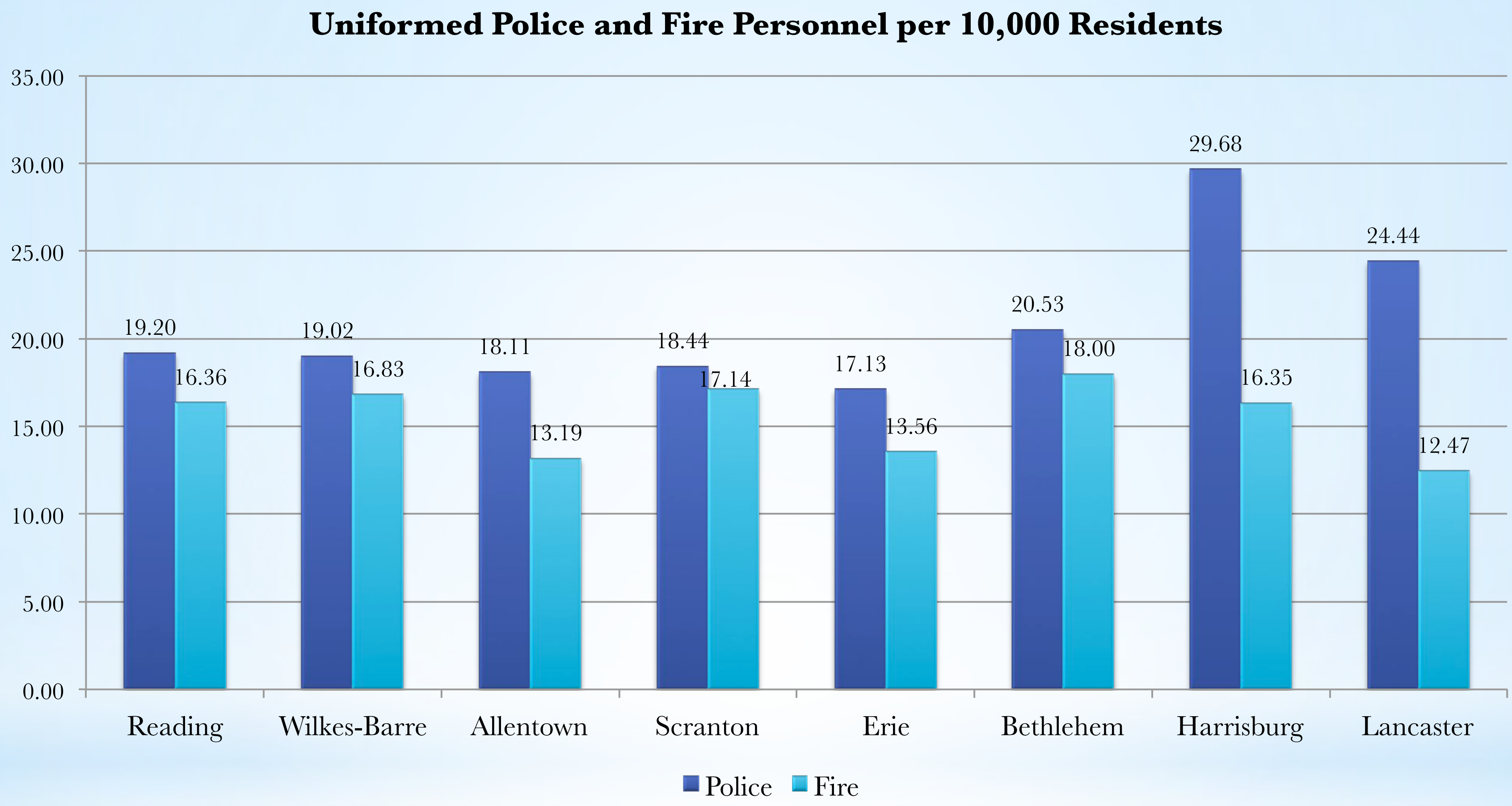
What Drives Costs?



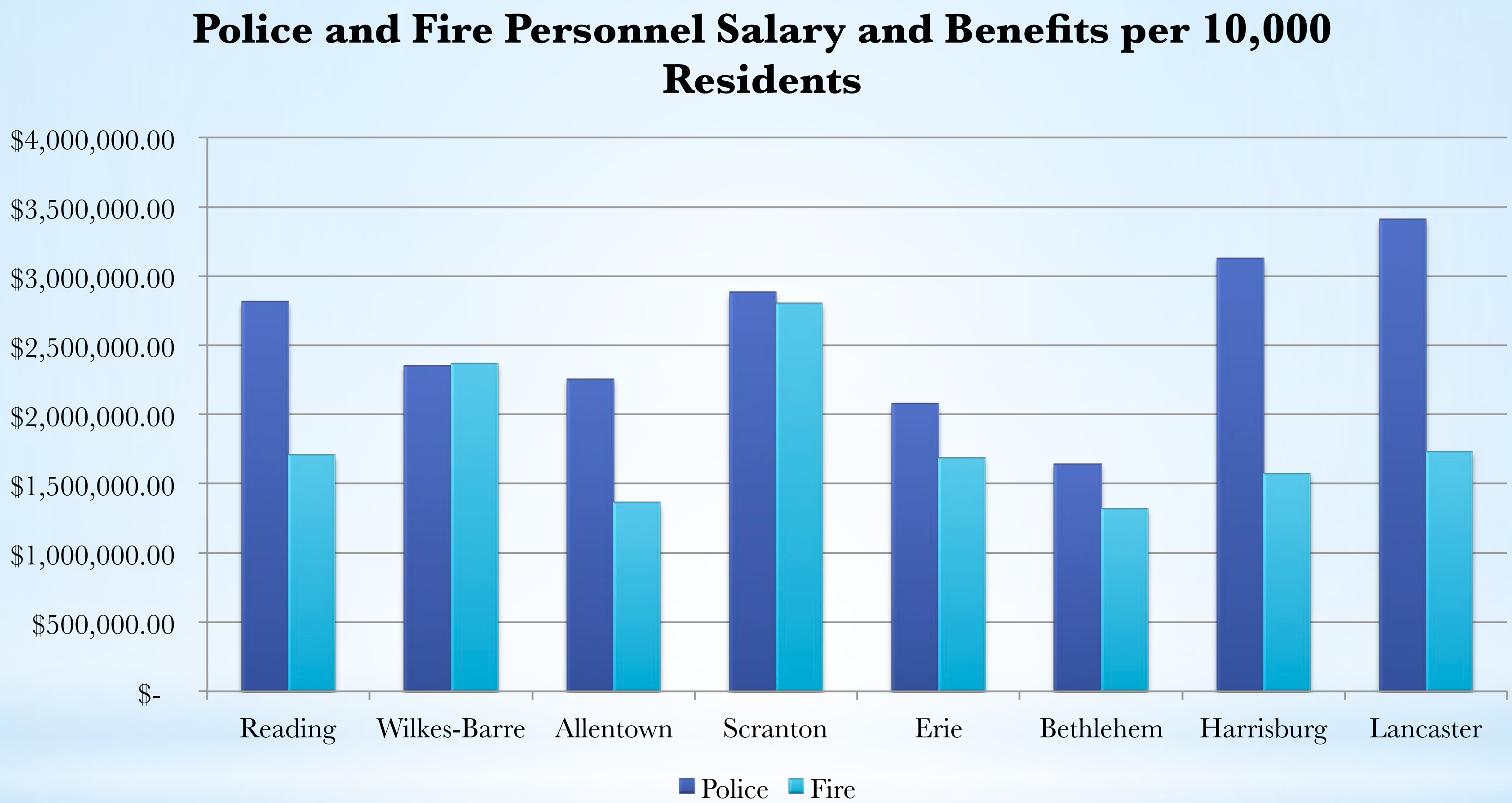
Rising pension, rising health care costs.



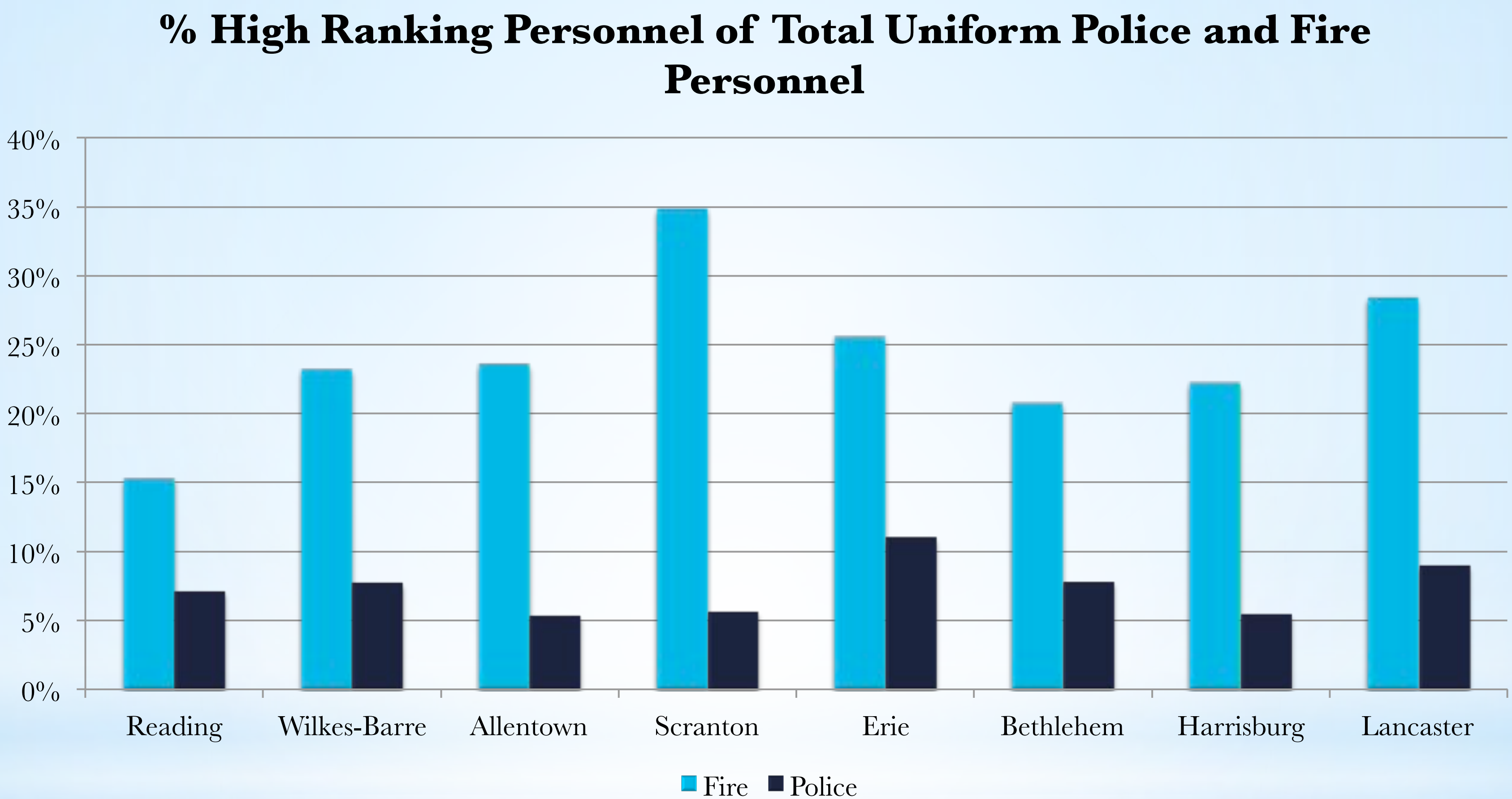
Police and Fire are by far the greatest contributor to personnel costs. Salary and wages increased since 2008—49 percent and 59 percent for Police and Fire respectively; pension expenditures grew by 261 percent for the Bureau of Fire and 451 percent for the Bureau of Police



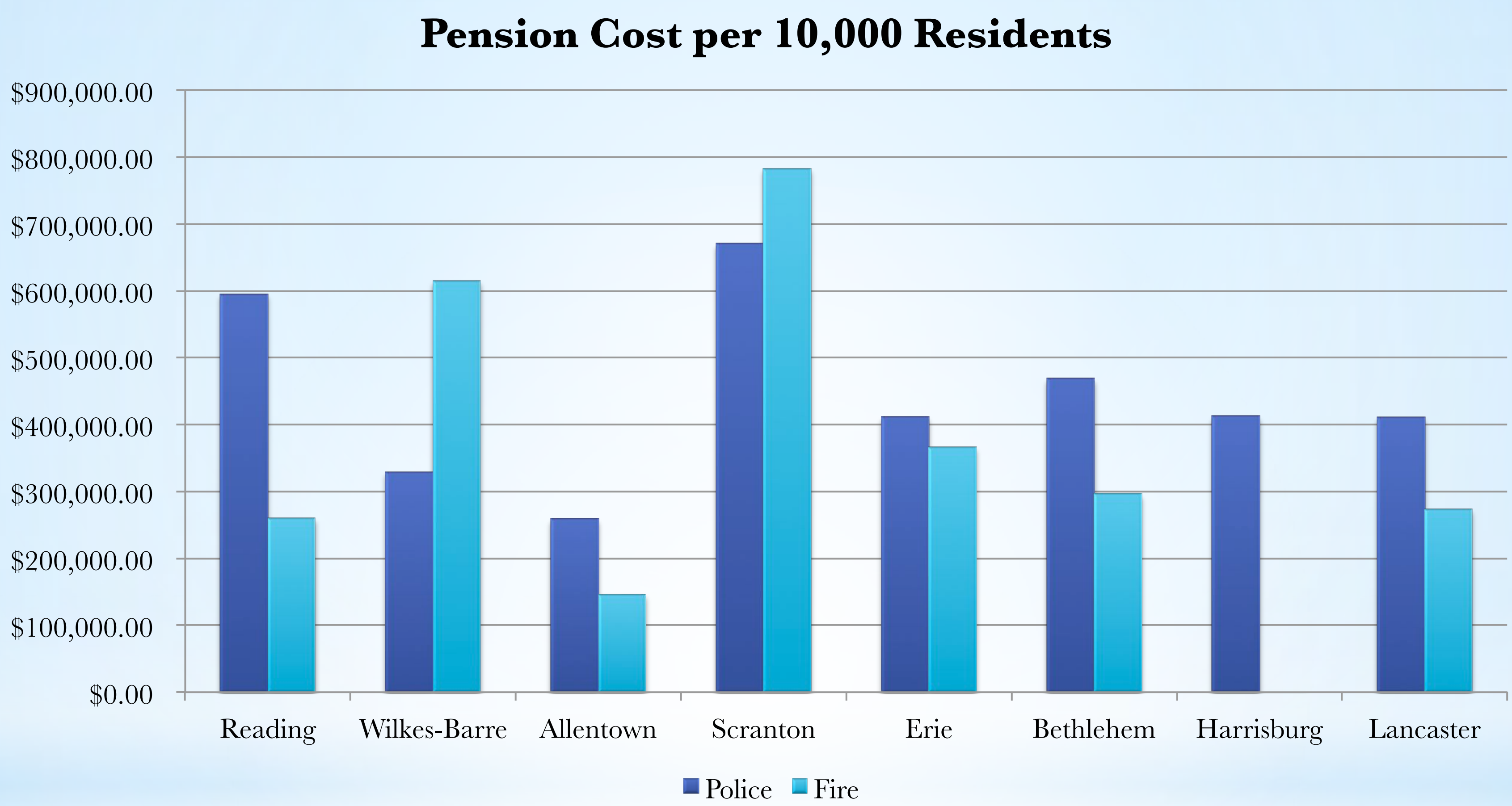
Scranton has fewer Police personnel than the average among its peer cities and more Fire personnel than the average. However, staffing is not far from the norm in either case



If Scranton's personnel numbers are not remarkably high, what accounts for the high *cost* of the personnel, particularly in the Bureau of Fire?



Reason One: Scranton's Bureau of Fire is too "top heavy" the above shows the % of the Bureau's personnel holding the rank of lieutenant or greater. This should be addressed during contract negotiations, which we suggest should begin far earlier than the scheduled time in 2017—truly ASAP

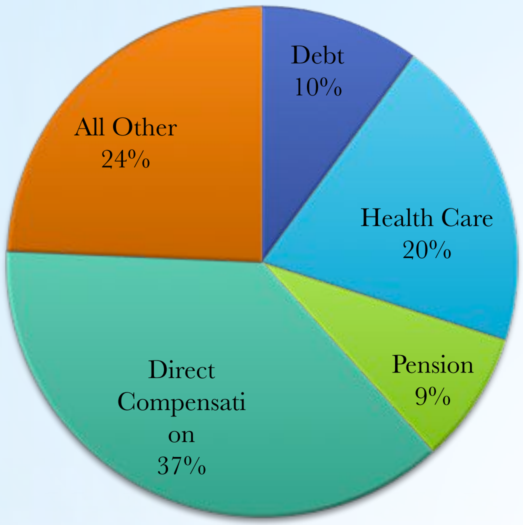


Reason Two: Pension costs are far too high.

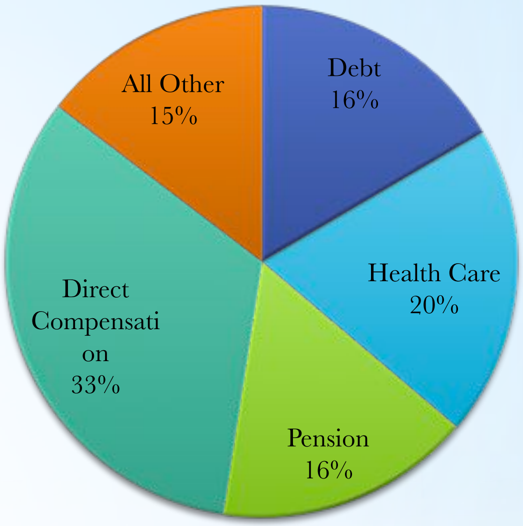
* Between 2006 and 2014, the pension appropriation grew by 153 percent
* By 2016, which is projected to mark the next significant increase in the City's MMO, due to the end of smoothing, the MMO will have grown by 209 percent.
* Payments to the pension funds account for 14 percent of 2014 appropriations

What Drives Costs? The Pension

City Expenditures By Category (2006)

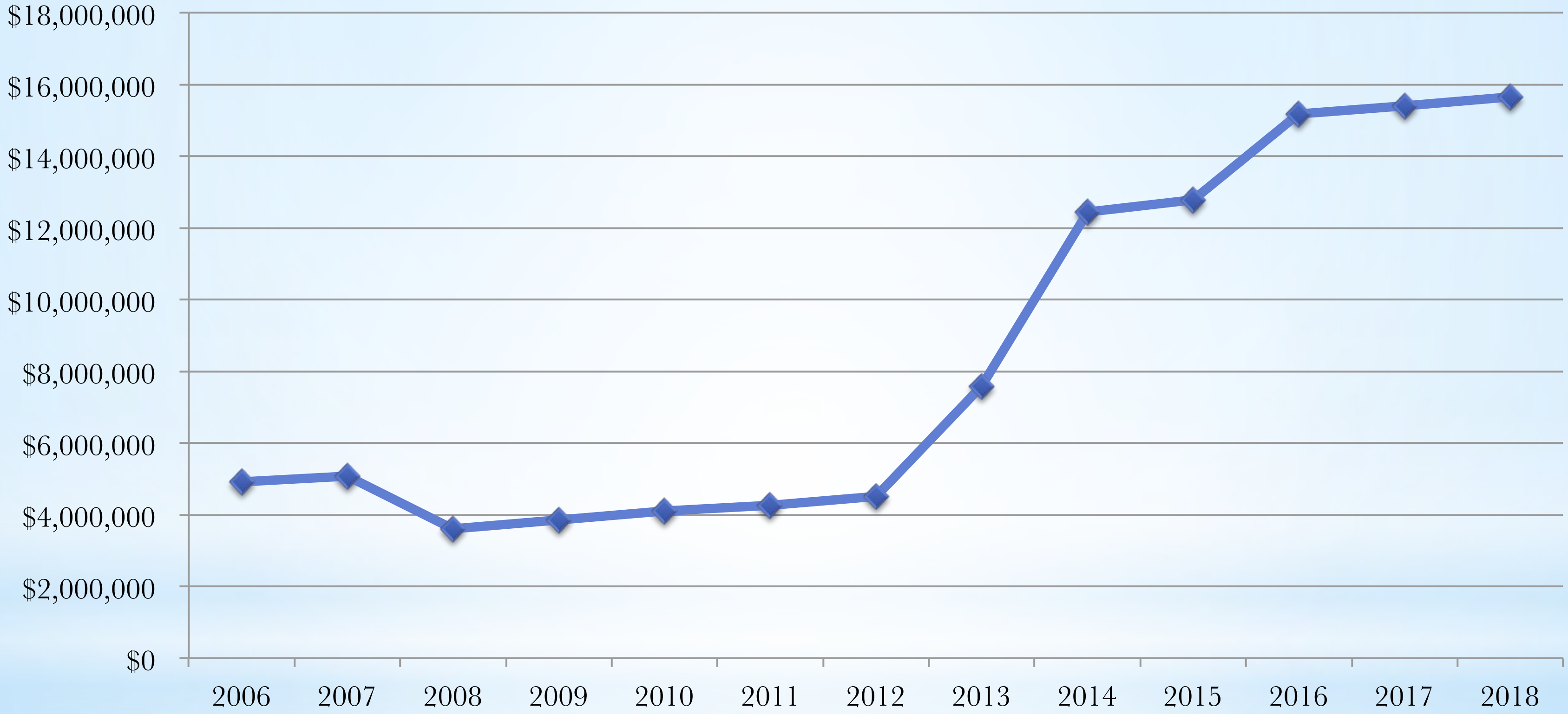


City Expenditures By Category (2018)

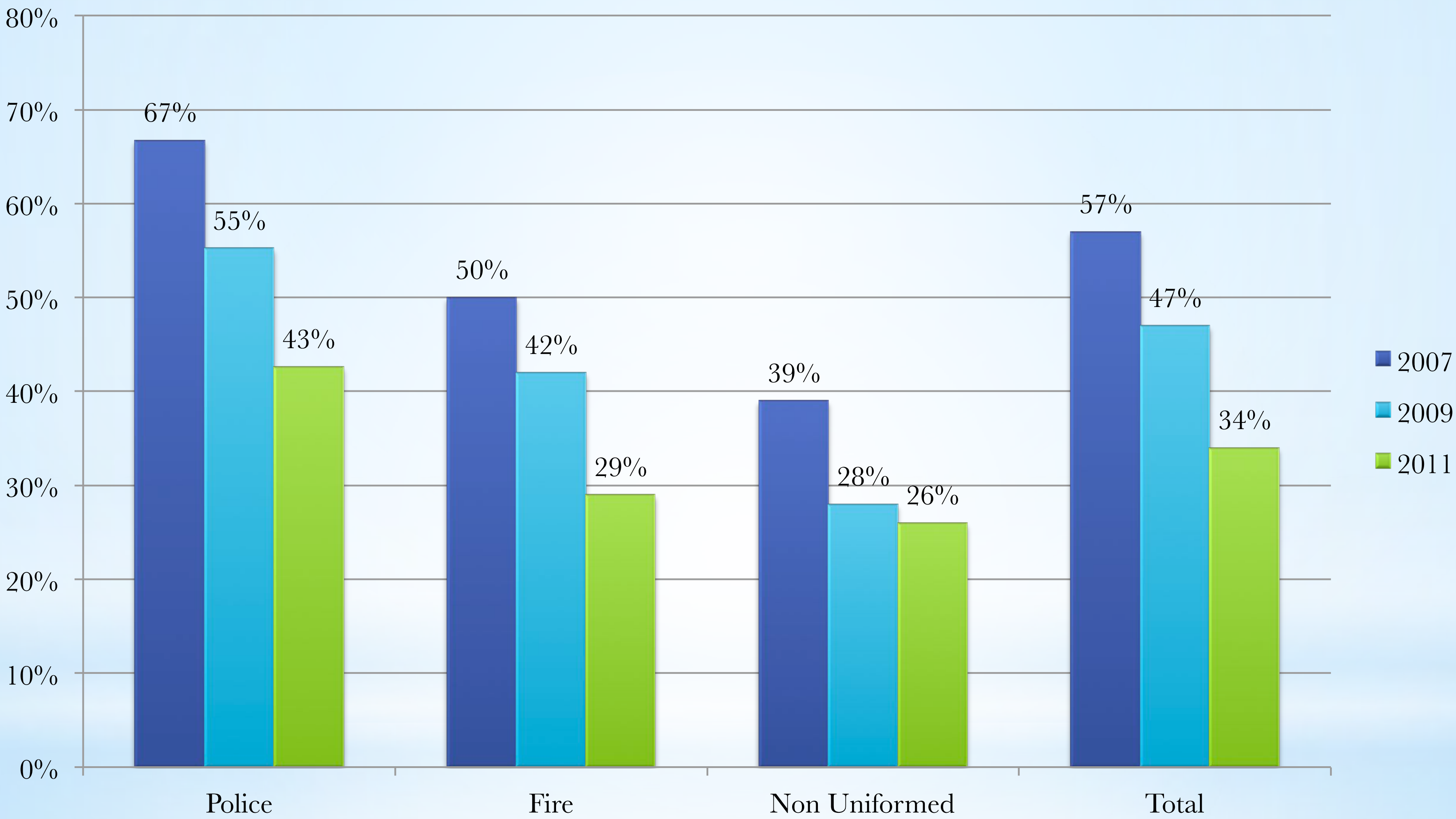


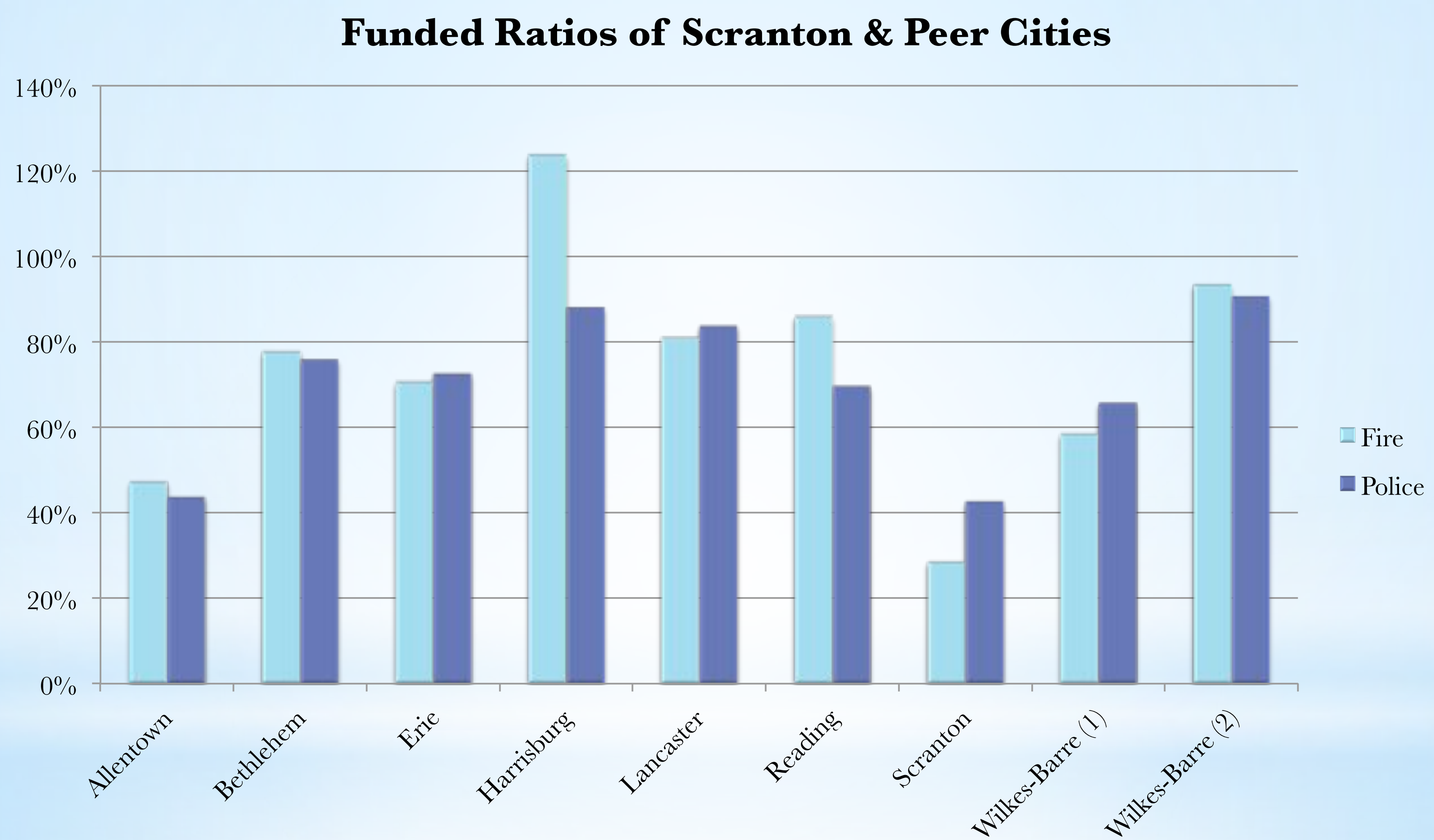
The pension payments and debt (we'll come back to debt later) comprise an increasingly significant proportion of the City's budget.

Growth in the Minimum Municipal Obligation (Pension Payment)



% of Assets to Liabilites in the City's Pension Funds

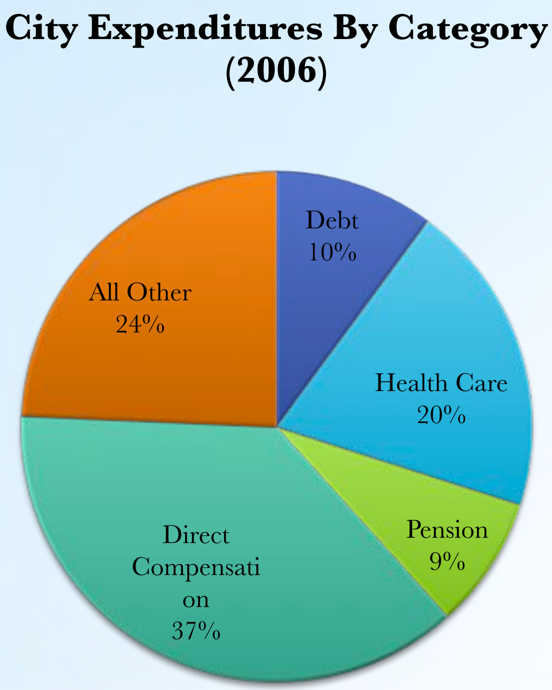


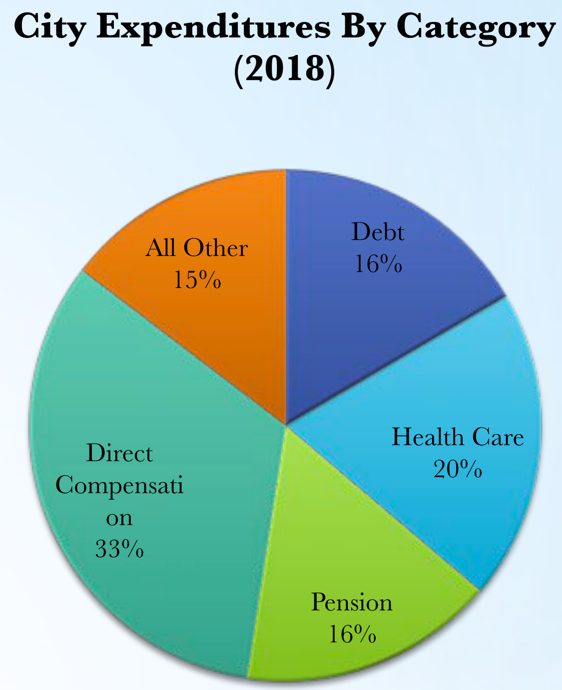


Funded Ratios of Scranton & Peer Cities
140%
120%
100%
80%
60%
40%
20%
0%
Allentown
Bethlehem
Erie
Harrisburg
Lancaster
Reading
Scranton
Wilkes-Barre (1)
Wilkes-Barre (2)
Fire
Police

Strategies: Pension

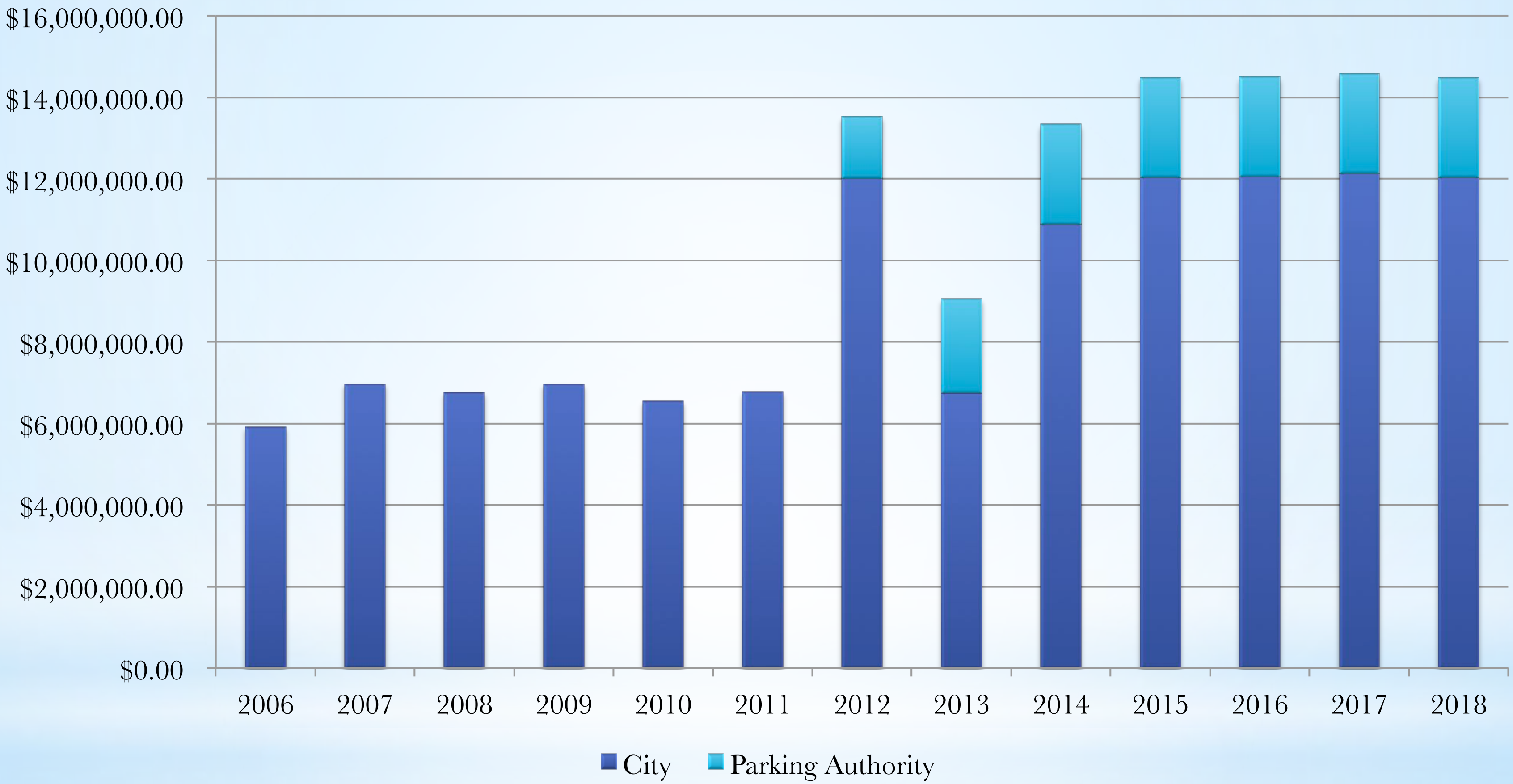
* Monetize select assets in order to make a significant one-time payment into the pension funds
  * The Scranton Sewer Authority.
    * Outright sale (public to public transaction)
    * Long term management contract
    * Good policy
    * A sale of the Scranton Sewer Authority, which *nets* the City $20 million could save the City approximately $1.5 million on its MMO annually, should other variables related to the pension hold
* Act 205 Non-Resident Earned Income Tax
  * Only for pension funding; can only stay in place as long as pension is "severely distressed"
  * ¾ of a point brings in $5.1 million in first four quarters of collection
  * More than 40 municipalities in Pennsylvania have this tax and it has existed for over 25 years
  * More than half of Act 47 municipalities have a *non*-Act 205 non-resident earned income tax.
* Pension reform (focus on new hires)
  * Higher contributions
  * Changes to the age of eligibility and the calculation of benefits
  * Defined contribution benefit structure, hybrid defined benefit/contribution structure
  * Pursue legislation when appropriate



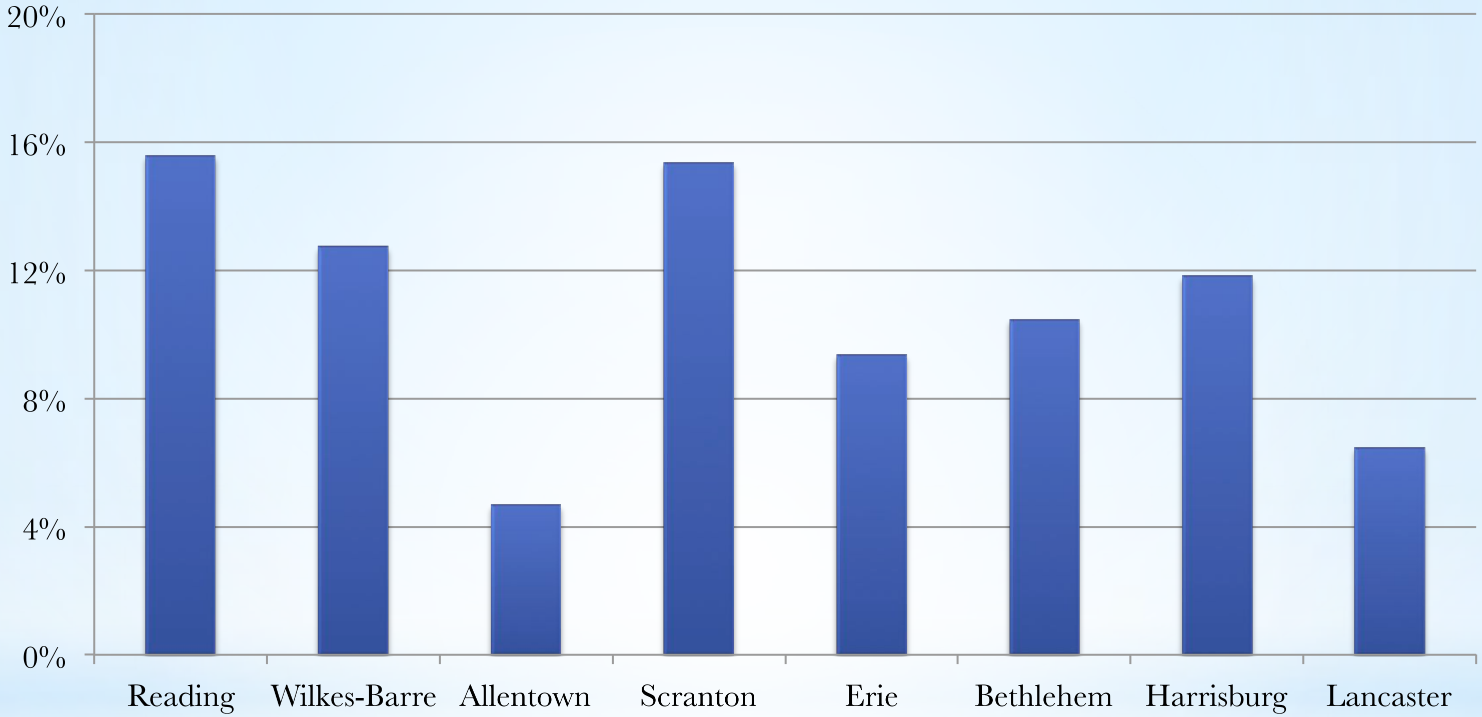


Once again, pension *and* **debt** comprise an increasingly significant proportion of the City's budget.

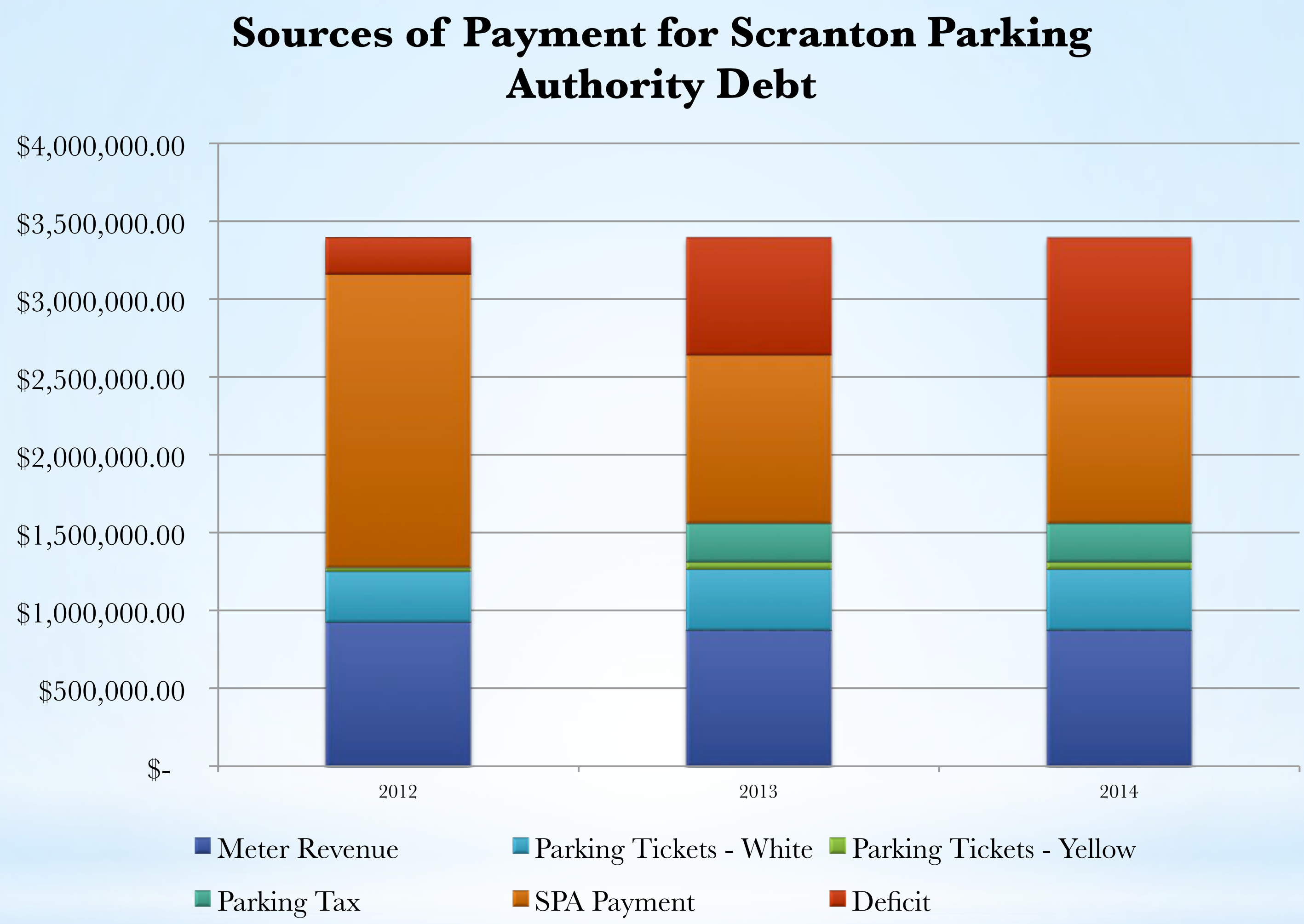
Historic and Projected Debt Service Payments



Debt Service as % of Total Expenditure, Excluding TANs (2014)



Target Debt Service Payments as % of Total Expenditure: 10-12 percent



The City guarantees the debt of the Scranton Parking Authority, which increasingly struggles to pay its own debts. Even if one were to pledge the meter, parking ticket, and parking tax revenues, as well as the current portion of direct SPA payments on the debt, a deficit of $900,000 would remain in 2014. This does not include the hundreds of thousands of dollars in immediately needed capital.

* Strategies: Debt

* Initiate the sale of the Scranton Parking Authority
  * This will leave about $31 million in residual debt assuming a $22 million sale, which is the latest appraisal
* Explore a broader debt restructuring, new debt issues
  * The sale of bonds to cover an initial $5 million payment on the judgment award
  * A restructuring of the City's Series B of 2003, C of 2003, and D of 2003 that would occur in Spring 2015.
  * A restructuring of the Scranton Parking Authority's residual debt after a sale of all parking assets, assuming a need to issue a general obligation bonds for approximately $31 million
  * The issuing of approximately $53 million in bonds to cover the approximately $22 million judgment and the residual SPA debt
* What can alternative market investors bring to the table?

	2015	2016	2017	2018
$53M	$1,550,000.00	$1,550,000.00	$1,550,000.00	$1,550,000.00
$5M	$1,300,000.00	$1,300,000.00	$1,300,000.00	$1,300,000.00
$53M w/ Savings	$250,000.00	$250,000.00	$250,000.00	$250,000.00
$33M	$(150,000.00)	$(150,000.00)	$(150,000.00)	$(150,000.00)
Savings on Current	$(1,300,000.00)	$(1,300,000.00)	$(1,300,000.00)	$(1,300,000.00)
$33M w/ Savings	$(1,450,000.00)	$(1,450,000.00)	$(1,450,000.00)	$(1,450,000.00)

Numbers in parentheses indicate a savings, but are not as comprehensive; these are rough estimates

* Potential (Savings)/Costs of New Debt Strategies

* The City will face increasingly large deficits in 2015, 2016, and 2017 if no action is taken. We project deficits of $8.6 million, $12.6 million, $14.3 million in those years, respectively (this assumes the $5 million payment on the judgment is made)
* The City needs to be able to close these deficits, provide additional funding to the pensions, and build equity to help pay for needed investments
* The City should also raise enough money—or find offsets through appropriation reductions—to fund a phasing out of the Business Privilege and Mercantile taxes
  * 25 percent reduction in year one, a 50 percent reduction from 2014 levels in year two, and a full elimination by year three.
* The table on the following slide shows our basic approach

Superfunding the Pension and Building Equity

	2014	2015 (18%)	2016 (6%)	2017 (4%)
Total Real Estate Tax Revenues	$27,943,903.00	$32,973,805.54	$34,952,233.87	$36,350,323.23
Act 205 (.75 pts.)	-	$5,109,549.09	$5,109,549.09	$5,109,549.09
LST	$1,650,000.00	$4,950,000.00	$4,950,000.00	$4,950,000.00
Increase				
Total Real Estate Tax Revenues	-	$5,029,902.54	$7,008,330.87	$8,406,420.23
Act 205 (.75 pts.)	-	$5,109,549.09	$5,109,549.09	$5,109,549.09
LST	-	$3,300,000.00	$3,300,000.00	$3,300,000.00
Total New Revenues	-	$13,439,451.63	$15,417,879.96	$16,815,969.31
Projected Deficit		($8,612,594)	($12,642,137)	($14,329,308)
Adjusted Surplus/(Deficit) with New Revenues		$4,826,857.63	$2,775,742.96	$2,486,661.31

* Cutting Health Care Costs
* Sharing Services
* Pursuing Budgeting Best Practices
* Innovative PILOTs
* Expanding Grants and Economic Development
* Exploration of a New Refuse Collection and Storm Water Authority

* Operational Improvements

*Review of Recommendations

* Immediately begin the process of initiating the sale of the Scranton Parking Authority in its entirety
* Reopen the City's contracts with its Collective Bargaining Units, focus on negotiating appropriate health care, and, especially, pension reforms (e.g., higher contributions, migration towards a defined contribution or hybrid plan for new hires, later pension eligibility dates), as well as changes to starting salaries, time between steps, and ranking standards/distribution. Determine the need for State legislation, if appropriate, for implementing negotiated reforms
* Establish an Act 205 tax, at .75 points, which allows the City to tax non-residents but *only* for purposes of funding the City's pension; this would raise $5.1 million in the first four quarters of collection. More than 40 municipalities in Pennsylvania have this tax in place; more than half of Act 47 municipalities have a *non*-Act 205 non-resident earned income tax.

* Assuming the passage of the Act 47 revisions, tripling the Local Services Tax Rate, which would raise $4.95 million ($3.3 million over the amount budgeted in 2014). A portion of this revenue ought to be directed towards covering debt related to the judgment, should the $5 million initial payment come to fruition
* Explore the sale or lease of the Scranton Sewer Authority in an offering to both public and private entities, subject to legal review. Upon the completion of the process, direct the entirety of the proceeds to the pension fund
* A property tax increase of 18 percent, 6 percent, and 4 percent in 2015, 2016, and 2017 respectively
* Thoroughly restructure a portion of the City's existing debt, the residual debt of the Scranton Parking Authority, and judgment-related debt.

* Phase out the City's gross receipts taxes (the Business Privilege and Mercantile Taxes) beginning with a 25 percent reduction in year one, a 50 percent reduction from 2014 levels in year two, and a full elimination by year three.
* Initiate a reassessment. The Mayor should make a formal request to the County either by letter or personal appearance, requesting the reassessment.
* Appoint a commission of various stakeholders and leaders from both government and outside government to develop a study on the implementation of various shared services programs
* Review the possibility of dissolving the Bureau of Refuse and migrating personnel to a new refuse collection and storm water runoff public authority
* Conduct a thorough review of the City's current assets
    * If it is determined that the City does not own an asset outright, the nature of its relationship to the asset should be carefully assessed and recorded.