Pennsylvania Intergovernmental Cooperation Authority

**Staff Report
on the
City of Philadelphia's
Five-Year Financial Plan
For
Fiscal Year 1995 - Fiscal Year 1999**

May 2, 1994

PENNSYLVANIA INTERGOVERNMENTAL COOPERATION AUTHORITY

1429 Walnut Street - 14th Floor, Philadelphia, PA 19102 -- (215) 561-9160 Fax (215) 563-2570

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INTRODUCTION

The submission by the City of Philadelphia of its Five-Year Financial Plan, Fiscal Year 1995 - Fiscal Year 1999 (including Fiscal year 1994) and including Technical Modifications as of May 2, 1994 (collectively, the "FY95-FY99 Plan" or the "Plan") marks the first half of both Mayor Rendell's initial term and that of the current City Council, and is an appropriate time to note both the status and direction of efforts to restore Philadelphia to fiscal balance. The 1992 approval of the Five-Year Financial Plan, Fiscal Year 1992 - Fiscal Year 1996 (the "FY92-FY96 Plan") was in many respects the "beginning" of Philadelphia's fiscal rehabilitation. As noted in prior PICA Staff reports, achievements in the intervening two years have been significant, although almost as illustrative of the depths to which the City had fallen as a functional government as they are indicative of advances.

The City, in the Introduction to the FY95-FY99 Plan, notes:

> While tightened managerial control over the past two years has succeeded in bringing current expenditures back in line with current revenues, without further change other forces will continue to drive up future expenditures faster than revenues. For all our successes,...there are external forces that continue to undermine our fiscal recovery.

The PICA Staff agrees (and has noted in its prior reports) that the City has made substantial progress in balancing its budget, and also recognizes that under- and unfunded State and Federal mandates continue to put great pressure on the fiscal capacity of Philadelphia, as well as other municipalities. Nonetheless, there is no guarantee that help from the Commonwealth or Washington is forthcoming - either in the form of mandate relief or greatly increased funding. The City properly has recognized that it is not prudent to form fiscal policy around the assumption that it will.

Notwithstanding demands placed upon the City by other units of government, with continued attention to control of personnel levels and departmental spending it is likely that Philadelphia will report a substantial operating surplus for the 1994 fiscal year. The outcome of legislative deliberations concerning the Commonwealth's budget (and accordingly the amount of funding which the City can expect to receive from Harrisburg for its 1995 fiscal year) is still speculative. Assuming, however, State funding within the range anticipated by the Plan, and continued fiscal restraint by the Rendell Administration, absent unanticipated events the FY95 budget should be balanced.

Structural Balance -- Budget and Plan

Is there an inconsistency between projecting a series of balanced budgets and facing the prospect of future deficits? PICA Staff believes the two concepts are not only consistent but illustrate the most fundamental risk to the City's efforts to truly "rehabilitate" its finances.

In any undertaking to gauge the City's prospects for long-term success, it is crucial to make a distinction between achievement of an operating surplus and a "structural balance" between expenditures and revenues. The New York State Financial Control Board (FCB), the fiscal oversight agency for the City of New York, has received well-deserved national recognition for its work with the concept. In a 1992 report, the FCB said:

> Structural balance is an abstract concept that describes a system of revenues and expenditures that is fundamentally consistent and can be sustained with reasonable reliability through economic expansion and recession. Sometimes circumstances change and a structure that used to be balanced is no longer balanced.
>
> ....
>
> A near-term balanced budget at the price of long-term balance is unacceptable, however. Clearly, the long-range stability and reliability of municipal services provided by a balanced fiscal structure must be the central objective guiding policy-makers as they identify and implement budget-balancing actions.

PICA Staff agrees with both that definition and the FCB's assessment of priorities, and has emphasized them in its prior reports.

The cash flow crisis which Philadelphia experienced between 1990 and 1992 has been addressed, but at the price of an additional debt burden which the City is obligated to factor into its budgeting (assuming that remaining Series of 1992 bond proceeds are allocated as anticipated in the Plan):

Purpose	**Amount** (million $)
Accumulated Deficit - FY91	$153.5
Productivity Bank - FY92	20.0
FY92 Deficit	71.4
FY94-Indemnities	23.5
FY95-Indemnities	7.8
Issuance Costs and Reserves	63.6
Total	$339.8

As the table above shows $339.8 million in *borrowed* money, the principal and interest on which is payable through the year 2003, has been used to buy time for Philadelphia to put its fiscal house in order, set the City's accumulated operating deficit at "zero" as of July 1, 1992 and provide substantial insulation against imbalance in the next two fiscal years as well. The City had no alternative but to seek PICA assistance, but any analysis of underlying fiscal reality must begin with the recognition that there was, and will be, a substantial price paid for the resources which the City used to create the opportunity to effect changes in the way Philadelphia manages its affairs. To put it in some perspective, the City will spend approximately $312 million, equal to about 68 percent of all the receipts it expects to receive from the 1 percent local Sales Tax, to fund debt service on deficit reduction indebtedness over the term of the Plan. An additional $162.7 million will be required to amortize the debt fully through its maturity -- $474.7 million in all (approximately $1.40 in debt service for each dollar borrowed).

PICA borrowing and the Sales Tax have given the City breathing room, and its own actions to collect revenues more aggressively, privatize some activities and achieve concessions in collective bargaining have produced both greater income and lower expenses than otherwise would have been the case. The Plan indicates that the net result of that effort, combined with actions yet to be taken, permits the City to anticipate a General Fund cumulative surplus at the end of FY99 of $56.598 million, less than .5% of City General Fund expenditures totaling over $11.9 billion over the life of the Plan. While it is likely that many of the initiatives included in the Plan are conservatively quantified, PICA Staff believes many of the revenue estimates to be somewhat aggressive absent significant improvement in the local and regional economy, and even under the most optimistic City estimates there is little room for error.

The long-term viability of the City's finances requires that the Rendell Administration at least meet the revenue projections in the Plan, and achieve a significant portion of the Plan's hoped-for economies. Particularly important to the integrity of the Plan is the City's assumed ability to avoid *any* wage increases after current labor contracts expire June 30, 1996. The final three years of the Plan fall after the expiration date of present collective bargaining agreements. If the next set of labor negotiations are as successful relative to the projections in the FY95-FY99 Plan as the current agreements were relative to the FY92-FY96 Plan (which properly was characterized as a very favorable result) could more than erase all of the Plan's projected accumulated FY99 surplus.

As noted elsewhere in this Staff Report, the Plan's underlying assumptions appear to be reasonable in the aggregate, although not free from risk. As in prior years, the City's FY95-FY99 Plan is dependent upon a variety of circumstances, many of which are beyond the City's control. The Rendell Administration has shown willingness both to control expenditures on an ongoing basis throughout the fiscal year and impose extraordinary measures when necessary to balance the budget. We have no reason to believe that they will not do so again in FY95 if such actions are required.

The City has represented, both in the Plan and elsewhere, that the FY95 budget begins to shift its primary focus from cost control to municipal services. In his budget address, Mayor Rendell said:

> ...with our first truly balanced budget since 1987, our departments will have the opportunity to invest in enhanced and, in many cases, expanded services. Next year's proposed budget, therefore, holds all departments harmless at this year's estimated spending levels, while actually increasing funding in certain key areas.

PICA Staff has some concern about Philadelphia taking a "hold harmless" approach in its budgeting. There remain great opportunities for cost reductions throughout Philadelphia government, and (as noted below) there are ambitious and potentially very successful efforts being made by the City to improve government operations and financial performance. As PICA Staff has noted in several reports, the question is not whether there is a desire on the part of the Administration to make changes, but rather whether departments have the commitment and capacity to both control expenditures and improve services. As Mayor Rendell emphasized in his campaign and in the initial five-year financial plan, if agencies are not challenged to save, and rewarded if they do (or disciplined if they do not), there is a question as to how much impetus for change there will be.

There is evidence of structural and managerial impediments to department-central administration cooperation in the effort to alter the fundamental operation of government and institutionalize change. The Administration deserves great credit for its development of the Monthly City Managers Report - a groundbreaking effort to compile and analyze information about City operations - but it only recently began distributing the Report widely to departments who could benefit from it. Initiative progress summaries included in the Managers Reports frequently have noted that departments have not cooperated in providing consistent information or reliable updates on the status of initiatives, and information included in the summaries frequently is inconsistent with other data. This may also be indicative in at least some cases of departments not having "taken ownership" of proposed reforms, and of the central administration not having taken full responsibility for the work product of departments. Changes in the Office of the Managing Director may offer some potential for improvement in this regard.

Mayor Rendell also noted in his budget address that City agencies must focus on the provision of services in addition to the control of spending. As was the case last year, due to admittedly limited capacity on the part of the City to quantify results, the Plan and FY95 budget only minimally rely upon initiatives, and PICA Staff has some concern that agencies will feel less of an obligation to meet either performance or spending goals if there is less downward pressure on budgets to force them to do so. The imposition by the Administration of "target spending plans" in the past two fiscal years has provided some flexibility to move funds among agencies to deal with the effect of lower than expected revenues and other situations, but the Administration has not yet indicated its intent in this area for FY95 and beyond. PICA Staff is concerned that the amount of future reductions (and related flexibility) might be substantially less than before.

This fiscal year, for the first time, the City has required agencies to both quantify their expected performance levels for FY94 and set goals for FY95. While most appear to have given the process little serious thought (as illustrated by most of the FY95 goals in most departments being little more than a copy of their projections for FY94), it represents the beginnings of an objective approach to policy making and the evaluation of service delivery. The effort is hampered by a central system which is as yet unable to quantify more than the most basic indicia of financial and management performance, and which does not have the capacity to allocate expenses to those who are responsible for them. Even with the potential for significant improvement in the near-term (particularly as noted below concerning the Mayor's Office of Information Services), there is still a significant question as to whether adequate management capacity exists within City government to establish accountability - apart from technological constraints. Without a firmly-rooted system which *requires* accountability, the prospects for institutionalization of change are at best speculative. The City's success in meeting the challenge is dependent on vision, organization and managerial capacity.

Setting Standards -- City Taxes and City Services

In his January Mid-Year Economic Report, the City Controller urged a reduction in City taxes for FY95, and the Mayor has expressed the hope that he will be able to propose reduced taxes for FY96. The question of whether to adjust local tax rates is a policy judgment for elected officials, and is not a determination which should be made by PICA. The Authority, however, by its statute is specifically authorized to "...make factual findings concerning an assisted city's budgetary and fiscal affairs," and "...make recommendations to an assisted city concerning its budgetary and fiscal affairs."[1] City taxation clearly is a subject upon which the Authority may express an opinion.

If the City intends to lighten the burden on its taxpayers in FY96 and beyond, it should set clear standards as to what must occur before it will do so, and state with equal clarity the other changes in the budget and Plan which necessarily will be required if structural balance is to be achieved and fiscal balance is to be maintained. The symbolism of a balanced budget and reduced taxes for a city which was not long ago seen as a fiscal basket case is powerful. Given Philadelphia's still-fragile fiscal condition, however, it should not take the risk of instituting a tax cut in FY96 if there is ***any*** prospect of having to increase taxes in the foreseeable future. Even apart from

[1]Pennsylvania Intergovernmental Cooperation Act for Cities of the First Class (Act of June 5, 1991, P.L. 9, No. 6), Section 203(c)(2) and (3).

the very real threat posed to fiscal balance by labor negotiations which begin during the 1996 Fiscal Year, the linkage between tax reductions and budgetary impact must be clear and absolutely supportive of the conclusion that it is not even indirectly based upon either funds provided by PICA or accumulated one-year operating surpluses "rolled over" to an opportune moment. Unless that conclusion is defensible, any reduction could be seen as an action unsupported by either economic substance or fiscal rationality.

While the City obviously must calculate the immediate fiscal impact of such measures, it also should weigh the message changes in tax policy send to both citizens and observers of Philadelphia's finances apart from symbolizing a city "on the way back." Studies have shown that Philadelphia's tax burden is among the highest in the nation for both individuals and business, in part due to Commonwealth tax laws. By the same token, many citizens believe that City services are ***qualitatively*** inadequate, and it is clear to even a casual observer that a large portion of the migration from Philadelphia has occurred not only because of taxes, but as a result of perceived shortfalls in the entire "package" of City services (including public education) and the strained relationship between local government and those it is supposed to serve. The performance by the City of the task it has laid out for itself -- to not only arrest the deterioration of its tax base, but to reverse it -- will be judged by its success in addressing that perception.

For a Philadelphia family with annual wage income of $25,000, a reduction of .10 percent in the Wage/PICA Tax to 4.86 percent generates yearly savings of $25.00. Any money that goes into a family's budget, instead of that of government, represents more disposable income for it (and therefore less available for government spending) but when the family's reward is less than fifty cents a week there are some questions about costs, benefits and priorities. Absent consensus that services have improved materially (or that they will improve as a result of specific efforts in progress), the City takes a great risk that a tax cut will be seen as an acknowledgment that services will not improve in the near term, and at best will be institutionalized at their current level. As the City has noted in the Plan and in prior reports, its performance in quantifying projected results on initiatives, especially those that require complex and longer-term inter- and intra-departmental actions, has been uneven, and it is imprudent to rely upon them for critical items of budget- and plan-making. It is necessary to strike a balance between challenging managers to improve performance and building a budget which rests upon reliable assumptions.

FY95 -- The Challenge

Cutting taxes when the budget is but delicately balanced is good public policy only when well-developed strategies are firmly in place to make up for the effect of lost revenues. This can take the form of assured growth in other sectors of the revenue base or predictable reductions in future expenditures, but should not be based upon the anticipated effects of the City's efforts to stimulate the local economy (whether by virtue of the tax cut or otherwise). While it is likely that the Convention Center and alternate uses of the Philadelphia Naval Shipyard will generate new employment and new tax revenue, it is not a good basis for projecting additional compensatory revenues. To the City's credit, the FY95-FY99 Plan generally is based upon that which is now known, and the success of the Mayor's proposed economic stimulus program is not something upon which the Plan depends.

The Plan, by its own admission, does not now include sufficient predictable or long-term resources to support tax reductions at any point during its term. The City should use FY95 to refine its tax strategy in the context of its strategic plan and larger policy goals, key among them the achievement and maintenance of structural balance and a longer view of the critical elements which must be addressed to do so. It must continue its efforts to create and improve basic systems within government, and institutionalize changes which have been made. Of equal import is to continue initiatives supportive of the development of internal financial and management controls which permit City policy makers to know what is going on in the departments, and re-focus City government from a top-down bureaucracy to a more service-driven, customer-oriented organization. Integral to the success of that effort is imposing *actual* accountability on all levels of the government, which may be the most important goal of all.

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Executive Summary and PICA Staff Recommendation

In preparing this report, PICA Staff has focused on areas of risk to the Plan, and sectors of City government with particular opportunities for fundamental change. Necessarily, such an effort will emphasize potential negatives rather than enumerate positive developments, except in the context of other matters. PICA Staff believes that the Rendell Administration and City Council have exhibited responsibility and restraint in their work to address Philadelphia's fiscal problems, and acknowledges the difficulty in stimulating the bureaucracy to implement changes which in some respects assault the premises upon which much of the operations of City government have rested for generations.

Overview

Methodology and Staff Report Date. The Plan was submitted by the City to PICA on April 4, 1994, and under the PICA Act the 30-day period for review expires on May 4, 1994. Authority Staff has consulted with the City, both on the departmental level and otherwise, since the Plan was presented to City Council on January 13, 1994, and has referred to material presented to City Council and the Controller's Office, as well as information included in reports submitted by the City to PICA and other data developed by staff of the Authority. This report includes reference to materials received by the Authority through April 29, 1994, including the Monthly City Managers Report dated April 21, 1994 for the month ending February 28, 1994.

Under Section 5.07 of the Cooperation Agreement PICA agreed not to disclose information provided to it in confidence by the City with respect to negotiation of collective bargaining agreements and ongoing arbitration proceedings, and the Authority has followed that requirement.

Relationship to Future Plan Revisions. The City is obligated under both the Cooperation Agreement and the PICA Act to submit a revised Plan in the event it enters into a collective bargaining agreement, or receives a labor arbitration award, at variance with that which was assumed in the Plan. The Cooperation Agreement anticipates that the Plan must be revised to deal with a such matters within 45 days after declaration of a "variance" by PICA. Appendix A discusses the PICA Act and the variance correction process in detail.

Apart from labor-related revisions, or those required by declaration by PICA of a variance in the Plan in the future, the Plan is subject to mandatory revision on March 22, 1995 (100 days prior to the end of FY95). At that time, the City is required to add its Fiscal Year 2000 to the Plan and make any other alterations necessary to reflect changed circumstances. Under the PICA Act, the City may determine to revise the Plan at any time and submit the revision to the Authority for its review. Under the PICA Act, the FY95-FY99 Plan was to be submitted to PICA by March 22, 1994.

While it is understandable that the City was reluctant to change the date for final Council consideration of the Plan by two days to meet the statutory deadline (City Council's calendar established a March 24, 1994 final approval date), the subsequent delay in formally submitting the Plan to PICA (it was not submitted until April 4), a clear violation of both the PICA Act and the Cooperation Agreement.

Accounting Concerns. The PICA Act requires that a modified accrual accounting system be used in the preparation and administration of the Plan, in accordance with generally accepted accounting standards. Specifically, the Cooperation Agreement (at Sections 4.02(a) and (b)) provides:

> Estimates of revenues shall recognize revenues in the accounting period in which they become both measurable and available...
>
> Appropriation estimates shall include, at a minimum, all obligations incurred during the fiscal year and estimated to be payable during the fiscal year or in the twenty-four (24) month period following the close of the current fiscal year...

The Plan as submitted meets the requirements of the PICA Act and Cooperation Agreement.

Underlying Assumptions.

Previous PICA Staff Reports have noted an underlying concern about consistency in presentation, indicative of problems of coordination among agencies. The statements made in those reports, to the effect that data and projections presented for one purpose often are based upon different assumptions from the same data presented for other purposes and/or in other sections of the Plan (*i.e.*, inflation rates and prison population), continue to represent a fundamental flaw in the manner in which the preparation and internal coordination of the Plan is managed.

Tax Revenues

As with prior five-year financial plans, the FY95-FY99 Plan is optimistic about the growth in tax revenues over its term. The risk to the Plan in the area of tax revenues was lessened by the reduction of approximately $90.7 million in projected General Fund revenues over the Plan's term (more than all local Sales Tax collections for an entire fiscal year) during the Council deliberations and PICA's informal and informal evaluation of it.

Tax Revenue projections are generally modest, with annual growth over the course of the Plan ranging from 2.6 to 3.2 percent. However, this is still higher than the FY93 actual results and the estimated FY94 actual growth level of 2.7 percent (including the PICA Tax and excluding the Sales Tax to provide comparable figures). Moreover, some of this 2.7 percent increase is due to improved enforcement. The Plan assumes a general improvement in economic conditions over the next five fiscal years. While the economy appears to be recovering, there remains considerable uncertainty about the pace and extent of the recovery over the Plan and how it will affect City revenues.

With respect to the City's initiatives to improve tax enforcement, PICA Staff is concerned that these initiatives will succumb to the law of diminishing returns during the Plan period, which could reduce growth rates for all City taxes. These initiatives in recent years have improved the City's tax revenue growth rates, but their influence is likely to diminish as the number of delinquent and undiscovered taxpayers diminishes.

The Wage and Earnings Tax revenue projection in the Plan is based on assumptions concerning growth in the number of jobs based in Philadelphia and the average wage of these jobs. The projection assumes a slower rate of employment loss in each fiscal year of the Plan, which appears reasonable, since the rate of job loss in the City, according to the most recent estimates from the Bureau of Labor Statistics, declined in both 1992 and 1993. The projection for wages per job, however, is of some concern to PICA Staff. One source of this concern is the changing industrial make-up of the City and the possible shift in job growth away from relatively high-paying sectors such as health services to relatively low-paying sectors such as those related to tourism.

The Plan's Real Estate Tax projection assumes a modest recovery in the real estate market, both in the commercial and residential sector. While the residential sector shows signs of improvement, there is as yet no indication of improvement in the commercial/industrial sector. Particularly with employment declines likely to continue in future years, the assumption of growth in the commercial market could be somewhat aggressive.

Plan projections for the Business Privilege Tax are based on long-term trends. PICA Staff is concerned that the volatility of this tax makes a projection based on historical trends difficult. The Plan projects growth of 3.2 to 4.2 percent annually, which appears somewhat aggressive given the history of revenue growth since FY89 and the possibility for a decline in prior collections due to the diminishing impact of enforcement initiatives.

The Plan projects the 1 percent Sales Tax to grow at 4 percent in FY95 and 3.5 percent in FY96-FY99, which appears reasonable to PICA Staff in light of past trends. Nonetheless, the 1 percent local Sales Tax has experienced continuing collection problems at the State level, which have made it difficult for the City to project its returns accurately, and which in turn has made the base for future years' projections somewhat suspect. While progress seems to have been made, FY94 has been a "good news, bad news" year for the Sales Tax. The "good news" is that month-to-month variances seem to have stabilized, and the State liquor stores remitted approximately $1 million in Sales Tax to Philadelphia (which previously had been unaccounted for) and are now regularly remitting Philadelphia Sales Tax. The "bad news" was that the initial Liquor Control Board remittance came as a surprise.

Personnel

While significant savings have been achieved in the costs of wages and benefits since FY92, they are projected to increase more rapidly in the future. Costs for wages and benefits are projected to outpace the rate of growth of tax revenue by at least 3 percentage points in the last three fiscal years of the Plan.

The Plan projects few changes in departmental staffing levels after FY95. Contemplated staff reductions at the Atwater Kent Museum and the Betsy Ross House were initially and are still included in the Plan -- increases to Department of Human Services staff were added, after PICA questions, in the Technical Modifications dated May 2, 1994 (10 to 11 positions annually). PICA Staff notes that the formulation of a strategic plan for the City should assist in making the Plan a more realistic statement of the fiscal impact of the City's priorities over a five-year period.

The Plan assumes no salary increases in FY97, FY98 and FY99. Any additional salary increases resulting from negotiations or arbitration with the City's municipal unions will result in additional personnel costs, and will require other initiatives to maintain Plan balance. The growth in health benefits costs has been reduced in FY93 and FY94 as a result of new labor agreements and declining personnel levels. Future health benefits cost growth is projected to be much higher, since personnel levels are expected to increase slightly, and the cost of benefits will increase at rates tied to the regional HMO rates.

Questions still remain about the implementation and institutionalization of the various work rule and procedural changes which the City obtained in the collective bargaining and arbitration process, and the results of that process will do much to determine whether the concessions will be as meaningful as they could be.

PICA Staff in prior reports has expressed concerns about the Finance Department's use of its authority to control hiring as a primary way to control expenditures in the absence of well-developed systems to control expenses otherwise. The Administration's commitment to add capabilities to its management accounting and information systems is encouraging, and the City continues to show dedication to driving down the cost of overtime. The City, as all employers, has to balance the requirements of its tasks with a cost/benefit analysis of the cost of new employees versus the expense of overtime. The use of private contractors for some City services has reduced the City's overtime exposure, and the resolution of issues concerning lower starting salaries in the Police and Fire Departments has made baseline Class 100 costs more predictable for at least the 1995 and 1996 Fiscal Years. The absence of new initiatives in the Plan to expand the competitive contracting process, and the prospects for increasing employment levels in City government, indicate that the major portion of any economies which will come in the area of overtime must result from better management of complement. An improved system for management, reporting and allocation of costs is a tool of great value in this effort, and the delay in its implementation until 1996 is not encouraging over the short-term.

In its report on the FY94-FY98 Plan, PICA Staff wrote:

> The number of positions budgeted for departments have..., often been much higher than the actual number of positions filled at any point during the year. The budgeted personnel level becomes an upper cap on the number of positions and during the year departments must again justify their need to hire to fill them. The budget and Plan should reflect a policy determination as to the level of staffing which is necessary, rather than an upside target with departments thereafter forced to negotiate with central administration for resources. The practice is antithetical to the concept of letting managers manage their agencies. Too much time and effort is required to get something done in City government under the best of circumstances, without the additional burden of re-negotiating the budget with each department after its approval. Complement control is a device which is helpful if used judiciously in concert with a good management system with larger policy goals -- not in replacement of such a system.

PICA Staff is still of that opinion.

Strategic Planning

The City began its strategic planning effort in January of 1994, and it and its consultants have worked with both City agencies and a group of outside advisors. PICA Staff and members of the Authority had urged that the City undertake such a project with the goal of setting a course for Philadelphia to follow in the years immediately ahead, and to assess its priorities, assets and limitations in a clear and analytical manner. PICA Staff, in prior reports and most particularly in its commentary on the City's report for the first quarter of FY94, stated its suggestions for the strategic plan with some specificity.

The task of balancing the budget on a year-by-year basis appears to be largely in hand, although the fundamental changes which are necessary to permit the City to have a sense of longer-term fiscal predictability and structural balance have not yet occurred. A comprehensive and candid strategic plan, if linked to an equally clear list of performance standards and targets and a well-articulated implementation strategy, can be of great value in this regard. Such a plan cannot exist in the "vacuum" of City government alone. It is unrealistic to assume that the City can conduct its affairs as if it were isolated from issues of public education, housing, corporate decision-making, the regional and national economy and Federal and State policies. A Philadelphia strategic plan should state the underlying assumptions about those issues with clarity, the City's expectations and goals with respect to them and recognize the place each (as well as City government itself) has in the overall mosaic of our region.

Management and Productivity

Risk Management/Indemnities

Workers' compensation costs are projected to decline from $31.5 million in FY94 to $21.0 million by FY99. This large reduction in costs depends on improvements in medical evaluation techniques, employment and rehabilitation plans for injured employees, and the resolution of the current backlog of workers' compensation cases, which number at least 1,100.

Effective January 1, 1994, medical services for City employees injured on duty are handled through a contract with Comp Services, Inc. The contract is based on the number of active City employees and a capped fixed price per employee. The City has assumed that the number of employees covered under the contract will not change. The cost per employee is projected to increase between 3.5 percent and 4 percent annually over the Plan, based on an assumed increase of medical costs by 7 to 10 percent and 3 to 7 percent annual cost reductions due to medical utilization management and aggressive physical rehabilitation. As with any new initiative, there is uncertainty in this projection, and PICA Staff will monitor its progress as implementation proceeds.

The City's projections for indemnity costs involve some risks relating to the rate of settling cases, the proportion of cases that will settle with payment and the average level of payment that will be required for each case.

Capital Program

For the first time in recent years, the City of Philadelphia anticipates entering the bond market to issue general obligation bonds to provide partial funding for its capital program. While the level of such borrowing has yet to be established, the City anticipates that a combination of PICA and City borrowing will provide funding for a FY95 Capital Budget totaling $145.5 million.

PICA Staff has been less than favorably impressed by the pace at which PICA-funded capital projects progress and has frequently voiced its concerns as to capital program matters in the past. Insufficient staffing within the Department of Public Property's Architecture and Engineering Division recently has been offered as a reason for delays, despite PICA having provided the funding required to fill all the positions indicated as being vacant. PICA Staff remains concerned with this situation and continues to await a proper explanation.

PICA Staff requests for documented information about efforts to upgrade the City's project management capabilities continue to receive no response. Despite Departmental assurances that "critical path" or similar project management reports would be required of contractors in FY94, PICA Staff has no reason to believe that the Department has in fact imposed such a requirement.

Productivity Bank

As a general matter, PICA Staff has expressed reservations about the City's ability to administer a true "loan" program from the beginning of the Productivity Bank process. It now finds itself in the position of once again pointing out that the concept was flawed from its inception and relied upon a non-existent system to handle repayments. PICA Staff again urges the City to review the process and determine whether it has the capacity to administer the program as first articulated by the Administration and to make necessary changes to make the process credible.

Principal Operating Departments

Fire Department

Fire Department cost saving initiatives had little success in FY94, primarily as the result of the minimum staffing levels provisions of the Act 111 Arbitration award. The Administration has indicated that this portion of the award foreclosed it from saving approximately $5 million annually. The arbitration-imposed staffing requirements are now being appealed by the City.

Office of Fleet Management

The Office of Fleet Management's (OFM) projected vehicle acquisition expenditures over the life of the Plan are substantial, a dramatic change from the recent past when the vehicle acquisition program was reduced as a budget balancing measure. PICA Staff is pleased to see OFM's commitment to modernize the City's fleet, and is cautiously optimistic as to its ability to maintain the fleet properly.

At the close of FY93 OFM stated that it had narrowed down the site selection for a centralized maintenance facility to two prime locations and that site acquisition would be made in early-to-mid-FY94. To date no decision has been made as to the final site. Whatever the delays surrounding this initiative, the linkage between it and many of OFM's other efforts require that they be rectified immediately.

Department of Human Services

With respect to the Department of Human Services (DHS), there are risks on both the expenditure and revenue sides of the Plan. Expenditure projections assume that the proportion of children receiving purchased services who receive high-cost types of service will decrease, and that the cost per day of service for nearly all types of purchased services will not increase for the entire Plan period. These assumptions project overall obligation growth approximating 3 percent in each year from FY96 to FY99, which is well below historical levels (which were as high as 18.6 percent as recently as FY92).

Projections for intergovernmental revenues associated with DHS are based on modest growth rates that generally are equivalent to the growth rate of expenditures, which is a reasonable assumption. However, the FY95 base level appears to be overestimated, given the State Department of Public Welfare-certified needs-based FY95 budget for DHS. As a result, overall Plan revenues appear to be overestimated. A further cause for concern is the Commonwealth budget for FY95, which is based on a new source of Federal funding which faces major implementation hurdles.

<u>Police Department</u>

As in the past, the Police Department has had difficulty controlling overtime costs in FY94. The Police Department attributes these costs to special events and an inordinate number of winter weather emergencies. PICA Staff urges that the Police Department implement its special events reimbursement initiative in accordance with the guidelines established by the Mayor and President of City Council in order to recoup the overtime costs where appropriate.

Concern exists that President Clinton's proposed Violent Crime Control and Enforcement Act, by providing a subsidy for an increased police presence over the near term, could encourage establishing uniformed officer levels which could not be funded in the future.

<u>Department of Public Health</u>

PICA Staff believes that strategic planning for the City's District Health Centers (DHC) is a critical need. The Department of Public Health has devoted efforts toward positioning the Health Centers to continue to play a role in providing service to the Medicaid-insured population after the Medicaid program is shifted to a managed care structure. However, PICA Staff is concerned that more attention needs to be paid to what role the Health Centers will have under potential national health reform proposals and the shifting composition of Philadelphia's health care network. Under various national health care reform proposals the role of the District Health Centers within the City's health care delivery system is likely to change substantially. In any event, the City should rationally examine the premises which underly its current commitment to act as a direct provider of primary health care services.

Additional funding for the District Health Centers is provided in the FY95 operating budget and the FY1995-FY2000 Capital Program. PICA Staff is concerned about the rationale for making these investments when no strategic plan for the long-term future of the DHCs has been developed, and more limited reviews of staffing and support systems are still in progress.

PICA Staff also has concerns that additional resources may be needed to properly monitor the Philadelphia Nursing Home contract, which began January 31, 1994. Two staff are currently devoted to this role. Additionally, the growth rates for PNH pass-through revenue are significantly higher than corresponding expenditure levels, which suggests insufficient growth rates for other Class 200 expenditures.

Mayor's Office of Information Services

As a part of MOIS' Strategic Information Technology Plan for 1994-2000 a training and support strategy is being developed to address the growing needs of the City's computer users. In order to do this, MOIS has sponsored development of a computer learning center at MOIS' 1234 Market Street office. PICA Staff applauds this development but cautions that while the establishment of a computer learning center is vital, getting employees trained may yet be difficult, particularly since the power of MOIS to mandate that City employees take classes is not yet clear.

In order for the City to judge the productivity of each department and better allocate costs, PICA Staff has observed that significant improvements in the City's cost accounting system are needed. The Chief Information Officer and the Finance Director have indicated that the updated version of the City's existing financial and management information system, which is being installed in phases, should be able to address this need.

In the past, PICA Staff has been critical of the City not using project management programs to avoid time-consuming problems and increase the ability of management to gather and use data about its projects. PICA Staff is pleased to see the use of computer-based project management by MOIS.

Philadelphia Prisons System

The Philadelphia Prisons System (PPS) is working on two new facilities. The Curran-Fromhold Detention Facility, a new 2,000 bed institution scheduled to open in February of 1995, is currently under construction and is to replace the obsolete Holmesburg Prison upon completion. Construction of a new facility, hoped to open in mid-FY96 and intended to replace the House of Correction and its modular addition, is in the planning stage.

The Plan acknowledges that any delays in the opening of Curran-Fromhold will have a negative impact on PPS operations. PICA Staff, recognizing that the opening date has already been extended from September 1994 to February 1995 and that the project is subject to on-going contractual disputes, has strong reservations as to its timely opening.

In an attempt to offer more efficient and less costly health care to PPS inmates, the City privatized health services. Currently the Health Department and the Prisons System are using different prison population projections throughout the life of the Plan. While PICA Staff makes no attempt to judge which entity's projection is more realistic, it again points out that interdepartmental inconsistency has caused the City budget problems in the past.

Department of Public Property

Significant cost reduction is projected for space rentals, as the City vacates the 1600 Arch Street and 1650 Arch Street properties to reoccupy the Municipal Services Building. Little additional saving appears to be assumed in the space rental budget beyond that attributable to vacating those buildings. PICA Staff is concerned about the lack of a City-wide space plan to guide decisions about reducing space costs over the long term or to serve as a basis for expenditure projections in the Plan.

The Plan projects a decline in utility costs on the basis of a series of initiatives being coordinated by the Municipal Energy Office. These initiatives could pose some risk to the Plan given their early stages of implementation and the difficulty of estimating their financial impact.

The SEPTA operating subsidy projection in the Plan is based on the assumption that the City's share of the local operating subsidy will decrease. Negotiations with the suburban counties are still in progress concerning the allocation of the local subsidy share, and PICA Staff is therefore concerned about the inclusion of this speculative assumption.

The Rendell Administration is considering consolidation of building maintenance functions within an single agency during FY95. PICA Staff is concerned that additional funding beyond that contemplated in the Plan may be needed to provide a sufficient level of preventive maintenance for the City's capital facilities, in which hundreds of millions of dollars are currently being invested.

Revenue and Law Departments

The revenue collections initiative in the Law Department has been very successful to date, with the anticipated FY94 level of collections $20 million higher than in FY91. However, to maintain this high rate of collections, it will be necessary to maintain the rate of referral of delinquent tax cases from the Revenue Department to the Law Department. This will require progress on Revenue Department initiatives, as well as acquisition of hardware and software capability in the Law Department to allow the Department to access Revenue Department databases.

The Revenue Department's Tax Information Processing System (TIPS) promises to reduce collection costs and increase revenues to the City. However, the timetable for implementing TIPS has continued to slip, and revenue projections associated with this initiative have been revised downward. PICA Staff takes comfort from the increased involvement of MOIS in this effort.

The Additional Collections initiative in the Revenue Department involves four separate projects, all of which are performing well in relation to original FY94 revenue projections. However, revenue production from this initiative is below FY93 levels, and is likely to continue to decline as the limited pool of non-filers and delinquent taxpayers targeted by this initiative is further reduced.

Streets Department

The Plan projects that the Department of Streets' FY95 obligations will decrease by $21.8 million from FY94. This reduction is the result of lower cost waste disposal contracts and the expected closing of a trash transfer station. Waste removal is the Department's largest "purchase of service" (Class 200) cost, and the Department has a history of anticipating the removal of more waste tonnage than it actually handles. FY94 costs are currently 3 percent below those originally projected. Unless the growth rate increases appreciably, the ultimate costs of waste disposal will be lower than Plan's projections.

The Department's ability to meet its Plan projections depends in large part on its ability to become more efficient and implement cost saving initiatives, and the City Controllers Office and the Department recently completed a project to begin to establish a process to create performance standards and associated monitoring systems. Several Departmental initiatives have been delayed and unforeseen problems continue to occur. Street cleaning modernization has suffered litigation delays; radio system communication problems have delayed the geographic information system's anticipated savings; and the Department has indicated that lower than initially projected vehicle availability has caused less efficient operations and increased overtime costs.

Other Significant Concerns

The Philadelphia Economic Stimulus Program is a major Rendell Administration program which potentially could impact the rate of tax revenue growth contained in the Plan. However, no such impact has been assumed in the Plan. PICA Staff will review the Program in more detail once it has been approved by City Council, with particular reference to its potential impact on the Plan.

Revenues from Traffic Court fees continue to come in below estimates, due to reductions in the number of traffic violation citations issued, and lack of stringent enforcement. FY94 Traffic Court revenues are projected to be $5 million less than originally anticipated. PICA Staff is concerned that the increased enforcement measures which the First Judicial District plans to initiate may not be enough to meet revenue projections, given other legal and systemic problems.

Litigation challenging the $18 million annual payment received by the City from the Philadelphia Gas Works poses an $94.5 million risk to the Plan. PGW payments to the City in FY94 and beyond are at risk as a result of this litigation, under which the Commonwealth Court has halted the final FY94 $4.5 million payment scheduled for May 1, 1994.

Staff Summary

The FY95-FY99 Plan presents a reasonable prospect for balanced budgets for each year of its term.

PICA Staff believes that the City's revenue projections in the Plan are in some degree optimistic. The upturn in the national economy, and what appears to be a deceleration in the rate of job loss in the City, gives some reason to believe that the deterioration in the City's economic situation has moderated. Nonetheless, the Plan depends (particularly in the real estate market) upon events generally working out as anticipated. By definition, in that the budget and Plan rest upon such occurrences, the balance is delicate. The dedication and creativity which the Rendell Administration has shown causes PICA Staff to conclude that fiscal balance is sustainable, although a continuing commitment to the institutionalization of fundamental change is required if structural balance is to be found and maintained, and if City services are to improve in any material degree.

Staff Recommendation

PICA Staff recommends that the Pennsylvania Intergovernmental Cooperation Authority approve the Plan as submitted to the Authority on April 4, 1994, as supplemented by technical modifications as of May 2, 1994.

CAPITAL PROGRAM

Primary Areas of PICA Concern

- o Use of Facility Assessment Reports for Departmental Capital Budget Preparation
- o Project Delays Due to Insufficient Staffing Levels
- o Project Management - The City has not Demonstrated the Use of "Critical Path" or Similar Project Management Techniques
- o Future PICA Capital Funding - No PICA Staff Recommendation at This Time

Introduction

For the first time in recent years, the City of Philadelphia anticipates entering the bond market in FY95 to issue general obligation bonds to provide partial funding for its capital program. While the level of such borrowing has yet to be established, the City anticipates that a combination of PICA and City bonds will provide funding for a FY95 Capital Budget totaling $145.5 million. The bulk of the FY95 projects are in the Public Property (buildings and transit), Recreation (including Veterans Stadium) and Streets Departments. PICA Staff has not reviewed the FY95 Capital Budget components for PICA Act eligibility and does not make a recommendation for funding by the Authority at this time. Capital projects will be reviewed by PICA Staff beginning in May.

In its FY95 Capital Budget, the City has allocated (through the Department of Public Property) approximately $450,000 for facility assessment reports on City-owned properties. While assessment reports will provide only a base of technical and engineering information, PICA Staff is pleased with this first substantive effort toward a better planning progress. PICA Staff nonetheless will very closely review how past facility assessment reports have been utilized in the current planning and capital budgeting process before making any recommendation to fund the proposed facility assessments with PICA bond proceeds.

Facility Assessment Reports -- *PICA Staff will use previously prepared facility assessment reports as a guide in its review of proposed capital projects*

In previous reports, PICA Staff has criticized the City for a lack of proper capital budget planning and preparation. Partially as an attempt to correct this problem, the City had facility assessment studies performed on its Police and Prisons Department facilities. Historically the City has tended either to ignore or only partially utilize such reports in its capital budget preparation. PICA Staff's review process for

FY95 capital projects anticipated to be funded by PICA will include reviewing previous facility assessment reports and requiring that the City demonstrate their linkage with the City's FY1995 - FY2000 Capital Program. The facility assessment reports are intended to prioritize the urgency of projects and PICA Staff plans to use such prioritization as a benchmark in making recommendations. PICA Staff also intends to hold the City more accountable for recommended (and approved) projects, and fewer substitutions should be anticipated.

Insufficient Staffing Levels -- ***The Capital Program Office has stated that staffing shortages in the Department of Public Property has caused project delays***

PICA Staff has been less than favorably impressed by the pace at which PICA funded capital projects progress and has frequently voiced its concerns in the past. A recent explanation that delay of a project was caused by insufficient staffing levels within the Department of Public Property's Architecture and Engineering Division is an example of the reason for that concern -- PICA had provided funding for the vacant positions in its 1993 bond issue. PICA Staff continues to be very concerned with this situation and is still awaiting a proper explanation from the City. Future requests by the City for PICA funding of capital program administration will be more closely examined.

Project Management -- ***There is no indication that the City has improved its capacity to track the work of its contractors***

During its 1993 review of proposed capital projects PICA Staff again raised questions about efforts to upgrade the City's project management capabilities, specifically whether the Department of Public Property (DPP) had followed recommendations of the Mayor's Private Sector Task Force to install and use a project management program. DPP's response was that the Department had determined, at least for the short run, that it would be preferable to impose upon contractors the responsibility to prepare and maintain "critical path" or similar reports and make them available to the City. During PICA Staff review of DPP, the Department agreed to provide copies of three of the most recent project management reports received (other than Phase II Prisons, which uses a project management system imposed by the Federal court), as well as an extract from the Department's contract form requiring such reports.

Despite repeated requests for the promised information, no response has yet been received, and PICA Staff has no reason to believe that the Department has done what it represented had been done.

The less-then-candid response on the part of the City raises additional questions about a capital program which is already troubled. Absent documented evidence that the Department has either installed and begun to use its own project management program, or has incorporated such requirements into its contracts, PICA Staff will be reluctant to recommend that the PICA Board approve new projects.

Future PICA Capital Funding -- *No PICA Staff recommendation at this time*

Despite a recommendation for Plan approval, PICA Staff makes no recommendation on capital project approval at this time, and the City has not submitted a capital funding request. PICA Staff anticipates meeting with the City in the near future to discuss proposed projects in detail, along with the status of projects which PICA has funded in prior bond issues. PICA Staff, with the assistance of the City Controller's Office, the guidelines established in the PICA Act, facility assessment reports, previously submitted capital budgets, anticipated and historic cash flows and other supplemental information will make a capital funding recommendation to the PICA Board at a later date.

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SUPPLEMENTAL FUNDS

Primary Areas of PICA Concern	Primary Areas of PICA Concern
Aviation Fund o OTA and International Terminal Cost Centers o Parking Authority Revenues	**Water Fund** o Water Fund "Scoop Payment" o Lack of Current Financial Projections

Introduction

As with previous Plans, PICA Staff has the responsibility to review the City's Supplemental Funds (the Aviation and Water Funds) to determine their potential impact on the General Fund. The key areas that PICA Staff monitors in the case of the Aviation Fund are Outside Terminal Area (OTA) costs and International Terminal costs; in the case of the Water Fund the key area is the Water Department's ability to make the annual "scoop" payment to the General Fund.

While improved, the level of detail provided to support the Supplemental Funds section of the Plan continues to be inadequate. The Plan fails to project fund balances for the OTA and the International Terminal Cost Centers separately (the Aviation Fund components which could negatively impact the General Fund). Water Fund projections included in the Plan are those which were prepared in August 1993 in connection with the Water Department's sale of its 1993 bonds, without update or adjustment in the intervening six months.

Aviation Fund

OTA and International Terminal Cost Centers -- *Projections as to their operations are lacking*

The ending fund balance (all departments) for the Aviation Fund is projected to improve progressively throughout the life of the Plan. A negative FY95 fund balance of $3.6 million improves to a positive $1.1 million in FY99. The Airport's unrestricted operating cash, which buffers the City's General Fund from the prospective need to restore deficits in either the Outside Terminal Area or International Terminal Cost Centers, is claimed to be sufficient to cover contingencies and it is thus implied that the City's General Fund should not be negatively effected. If deficits occur in the OTA and/or International Terminal Cost Centers and there is insufficient unrestricted cash available to cover the City's contractual portion of any such shortfalls the City General Fund will have to fund such items. The Aviation Fund's projected long-term gradual improvement can be attributed to additional revenues in the OTA from the Airport Marriott Hotel and increased parking usage.

Airport Parking Authority Revenues -- *A decrease in net Parking Authority Revenues at the Airport could be detrimental to the General Fund*

The City and the airlines have agreed to share 50 percent of all profits generated from the Outside Terminal Area; deficits are similarly shared up to a maximum deficit of $2.2 million, and after that point remaining deficits are the responsibility of the City. The primary funding source for this cost center is the net Airport-related revenues from the Philadelphia Parking Authority, which have been projected to be $12 million for FY94. If revenues collected throughout the life of the Plan are maintained at this level the Outside Terminal Area should have no difficulties maintaining a balanced budget; however, should the projections fall short the Aviation Fund might be required to seek support from the General Fund. PPA's data are not helpful to an analysis of probable Authority transfers to the Aviation Fund, either during FY94 or any other year of the Plan.

Water Fund

The City's General Water and Sewer Revenue Bond ordinance of 1974 and an agreement between the Water Commissioner and the Director of Finance provide that if there is a balance in the Water Department's operating funds, that balance can be transferred to the General Fund. That amount is limited, however, to an amount not more than the least of Sinking Fund Reserve earnings transferred to the Water Operating Funds during the year, the amount of Water Capital Improvement Fund Earnings during the year or an established $4.1 million limit. This Water Fund payment is known as the "scoop" and is projected to be $4.1 million throughout the life of the Plan.

Water Fund -- *The Plan shows sufficient earnings for the Water Fund to make the annual scoop payment*

The calculation in the Plan shows sufficient earnings for the Water Fund to make the annual scoop payment. The Water Fund financial projections in the Plan assume a 4 percent annual rate of inflation throughout the life of the Plan, which is at variance with the 3.5 percent general inflation rate used elsewhere in the Plan. The Water Department has built the scoop payment into its operating costs.

TAX REVENUES

Primary Areas of PICA Concern

- o Diminishing Returns on Enforcement Initiatives
- o Plan Methodology for Projecting Wage and Earnings Tax
- o Long-Term City Employment Prospects
- o Impact of Changing Industry Structure on Earnings Growth
- o Suburban Withholding
- o Projected Recovery in Real Estate Market
- o Volatility of Business Privilege Tax Trends
- o Sales Tax
- o Aggressive Assumption for Real Estate Transfer Tax

Tax Revenues Projections FY94-FY99 (millions)

Tax	FY94	FY95-FY99
Wage and Earnings	$ 812.7	$4,418.6
Real Estate	336.1	1,776.0
Business Privilege	225.9	1,261.8
Sales	82.0	457.3
Real Property Transfer	40.0	207.0
Tax Review Board	0.0	7.0
Other	59.4	324.8
Total	$1,556.1	$8,452.5

Introduction

The City's revenue projections for FY94, which form the base for the Plan's revenue projections, have not changed significantly from its first FY94 Quarterly Report. The first Quarterly Report's projections were revised downward from revenues originally anticipated in the FY94 budget in recognition of continued weakness in Philadelphia's economy. The situation has not changed substantially since that time, and the overall projections for FY94 appear reasonable.

Continued erosion of the City's employment base and at-best slow growth in the real estate market pose risks for the Plan. The Plan generally projects a modest recovery from recent trends (the beginnings of which can now be seen in current data), but a high degree of uncertainty remains about the pace and extent of the recovery that can be expected during the FY95-FY99 period. The City continues to lose jobs, although at a reduced rate from previous years. The City's residential real estate market may be stabilizing, but the commercial real estate sector shows little sign of improvement.

The Plan notes that Philadelphia's tax base has grown at rates below inflation each year since FY89. The base was increased only through the imposition of a new tax, the 1 percent local Sales Tax, during FY92. In the short term, there are various ways to increase revenues, such as rate changes, improved enforcement, increased fees, and new taxes, but as long as the underlying tax base continues to grow at a rate below the rate of inflation, achieving structural balance will be difficult.

Impact of Enforcement -- *The prospect of maintaining growth rates is unclear*

One area of PICA Staff concern is that improved enforcement initiatives may be contributing disproportionately to the growth in City tax revenue in FY94. For example, prior collections of Wage, Earnings and Net Profits Taxes (both City and PICA portions) for the first nine months of FY94 were 29.6 percent higher than in FY93, while current collections are estimated to be only about 2.5 percent higher. This reflects the impact of the City's enforcement initiatives. The heavy reliance in FY94 on enforcement initiatives to reach the City's revenue targets could pose a problem in the future as the potential for these initiatives to continue to increase revenue is reduced. While the Plan generally projects zero growth for prior collections after FY94, there is some question as to whether even the FY94 level can be maintained.

PICA Staff, in prior reports, has expressed its concerns about whether the enforcement initiatives would at some point fall victim to the law of diminishing returns with a coincidental decline in revenue growth. One such concern is that recent increases in prior collections may have resulted from a disproportionate reduction in the backlog of delinquent taxes, and that such gains cannot be sustained as the backlog is reduced and larger taxpayer liabilities are resolved. Another concern is that if a higher rate of collection of current taxes is achieved, it will reduce the annual yield that can be expected from prior taxes. Also, improved enforcement results primarily in a one-time gain, after which growth rates are reflected the growth in the underlying tax base.

PICA Staff's concerns would be less pronounced if the City's projections would separate the impact of revenue enforcement initiatives from the impact of growth in the underlying tax base (albeit broadened by adding former scofflaws). As a track record for these initiatives and new computerization initiatives develops it may be possible to better quantify this effect and include it in projections.

Wage, Earnings and Net Profits Taxes -- *FY94 projections appear on target*

Wage, Earnings and Net Profits Taxes totaled $1,005.9 million in FY93, and are projected at $1,026.0 million in FY94, an increase of 2 percent. This figure includes both the City and PICA portions of these taxes. It is important to consider the City and PICA portions together, since beginning in FY94 the PICA share of the tax was corrected to reflect a more accurate resident - non-resident apportionment. As a result of the recalculation, trends between FY93 and FY94 in either the City or PICA portion alone do not indicate the trends in the underlying tax base accurately. Also, any comparison should be based on the gross PICA Taxes, not the PICA Tax net of debt service, in that a portion of the PICA Tax is used to pay PICA debt service prior to being remitted to the City.

Through March of 1994, collections of the City and PICA portions of the Wage, Earnings and Net Profits Taxes were $759 million, an increase of 3 percent over the same period in FY93. This indicates that the City should achieve its current projection for these taxes in FY94. Revenues in the first quarter of FY94 were 1.2 percent above the first quarter of FY93, second quarter revenues were 3.5 percent above the second quarter of FY93, and third quarter revenues were 3 percent over the same period in FY93.

Plan Methodology -- ***While improved, the City's stated assumptions and methodology underlying its projections of Wage and Earnings Tax require further refinement***

The Plan bases its projection of Wage and Earnings Taxes on two forecasts: employment in the City and earnings per job. The result of the combination of the two forecasts is a projection of growth in earnings associated with jobs located in Philadelphia, and this growth rate is the assumed growth rate which has been used in the Plan for Wage and Earnings Tax revenues. The City's effort to state a rational and consistent set of assumptions and a related methodology has improved significantly over prior Plans. As noted below, the projection for employment appears reasonable given the most recent data which suggests that the rate of employment loss is moderating. The Plan's projection for average earnings per job, however, could be aggressive if employment losses in manufacturing, combined with stabilized employment levels in some high wage sectors and growth in lower paying service industries, depress growth in average wages.

Aside from the issues of whether the projections of employment and average earnings per job are reasonable, there is a limitation to the City's approach to projecting the Wage and Earnings Taxes since these taxes are based upon both income earned within the City by non-residents and income earned by City residents wherever they may work. Approximately 62 percent of Wage Tax collections derive from City residents, and an estimated 113,000 of these residents, a significant portion, are not employed in the City. As a result, the Wage and Earnings Tax should not be projected only on the basis of income earned at businesses located within the City, but should also take into account the earned income of all City residents.

U. S. Bureau of Economic Analysis data indicate that the earnings of Philadelphia residents ("earnings by place of residence") have been growing more slowly than the earnings of individuals employed in Philadelphia ("earnings by place of work"). Between 1980 and 1991, Philadelphia earnings by place of residence grew 65.2 percent, compared to 74.9 percent growth for earnings by place of work. This means that the portion of the tax base (either the number of people or their compensation) attributed to City residents who work outside of Philadelphia very likely grew at a slower rate than the portion attributable to resident and non-resident workers in the City. If this trend continues, a projection of Wage Tax collections based only on projections of earnings by place of work may be overstated.

City Employment Levels -- *The rate of employment loss appears to be moderating, but the impact on personal income and related tax revenue from continuing changes in the industry structure of the City is reason for concern*

The Plan projects a moderation in the rate of employment decline in the City. The Plan's assumptions are that the City will lose employment at the rate of 2 percent in FY94, 1.5 percent in FY95 and FY96, 1 percent in FY97, and 0.5 percent in FY98 and FY99. Recent data from the Bureau of Labor Statistics (BLS) indicates the Plan's projection for a lower rate of employment loss in comparison with recent years is reasonable. The most recent rebenchmarking of BLS non-farm payroll employment estimates for the City suggests that the rate of job loss in the City is moderating.

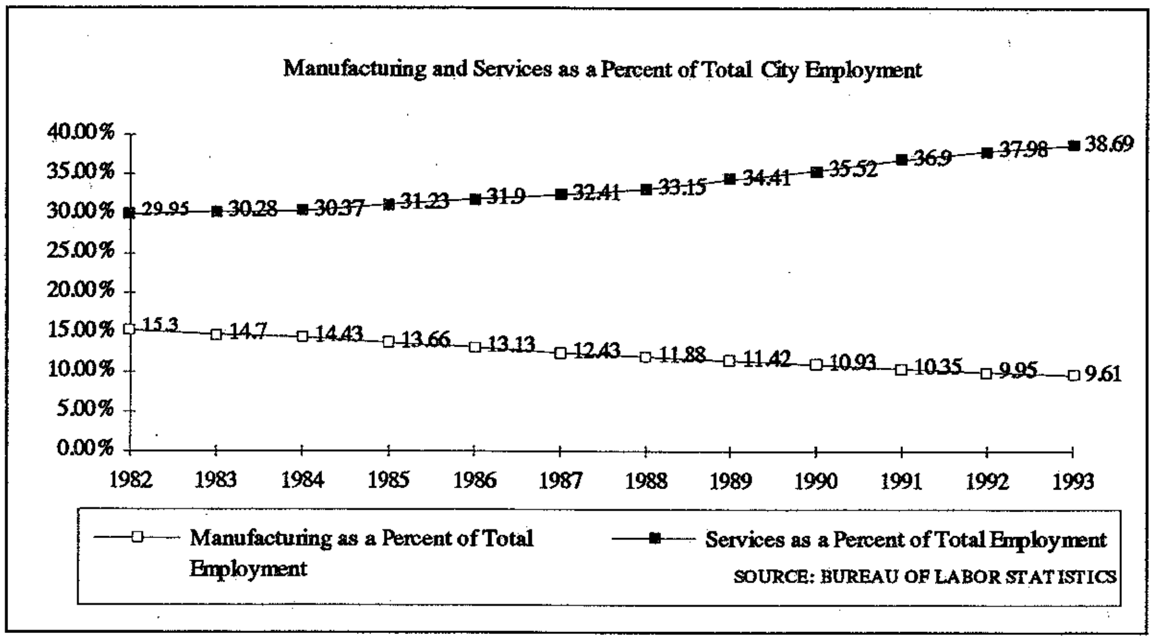
BLS survey data are re-benchmarked annually to reflect more comprehensive counts of employment as they become available. According to the recently benchmarked data, the average monthly number of nonfarm payroll jobs in Philadelphia for all of 1993 was 687,000, compared to the estimate of 678,000 prior to rebenchmarking. The revised data indicate employment loss in the City of 1.24 percent between 1992 and 1993, considerably better than the 2.6 percent decrease previously indicated. On that basis, job loss in 1993 was the lowest in percentage terms since 1988. Still, employment in the City continued to decline: in 1993, average employment in the City was 687,000, an 11.5 percent decline from the 1988 level of 775,900.

The moderation in the rate of decline in employment suggests that the national recovery may be effecting the City. In recent post-recession periods, the City began to see an increase in employment levels when national net new job figures rose above 2 percent. While a cyclical upturn should improve the City's employment outlook in the short-term, there remains a long-term secular trend of declining employment in the City that has existed at least since 1969. The City's rate of job loss in 1993, 1.3 percent, equals the average annual employment loss since 1969. The key question for the Wage Tax projection over the life of the Plan is how two effects -- the local impact of a national cyclical recovery and a long-term secular trend -- will combine to produce a net impact on City employment during the FY95-FY99 period. The goal of the City, in its proposed Economic Stimulus Program and otherwise, is to attack the secular trend.

Long-Term City Employment Prospects -- *Projections of earnings per employee appear to be based upon the assumption that "all jobs are created equal"*

The Wage and Earnings Tax revenue projection assumes that the average earnings per job will increase 4 percent each year over the course of the Plan. A key factor influencing the accuracy of that projection will be future changes in employment by industrial sector. Philadelphia's industrial structure is changing rapidly. Through periods of declining and increasing aggregate employment since 1982, one trend has remained constant: the increase in the share of City employment made up of services, and the decrease in the share made up of manufacturing.

Philadelphia employment declined through the early 1980's, increased from 1984 to 1988, and has declined in every year since 1988. Despite these changes in the trend of overall employment growth, in every year services have continued to make up a larger portion of the overall employment base while manufacturing has made up a smaller portion, as indicated in the chart below.



Despite a total City employment loss from 1988 to 1993 of 88,900, or 11.5 percent, services employment largely has bucked the overall trend since 1988. In fact, December 1993 City employment in the services sector was at an all time high.

As these changes have continued, average earnings per employee have increased at a rate of 5.5 percent since 1982, which is higher than the 4 percent growth projected in the Plan. However, there are some factors which could adversely affect this trend in the future. In the near future, the City may lose a number of relatively high paying jobs at the Philadelphia Naval Shipyard. Also, the nature of job growth in services may change from the trend of the 1980's. Health services job growth may form a smaller portion of the overall services job growth and a larger portion could be made up of growth in hospitality industry employment. This could be a concern for projections of Wage Tax revenues, since health services is one of the highest paying service sectors, while many of the jobs created in the hospitality industry are likely to be relatively low paying. These factors are noted below:

- o Closing of defense facilities. With the projected closing of the Philadelphia Naval Shipyard in 1995, it is possible that approximately 6,000 direct jobs and indirect employment related to these jobs will be lost to the City. City and regional leaders have begun efforts to develop plans to preserve employment at the Navy Yard -- either through other Navy uses or otherwise. It is thus likely, at least over the short-term, that significant tax revenues will be preserved. The important issue for Wage Tax projections is the overall level of earnings that will result from new enterprises at the Navy Yard.

- o Consolidation and rationalization of the health services industry. The course of health services is a key factor in determining Wage and Earnings Tax revenues. Health services had a very positive influence on City employment and earnings trends in the 1980's. According to U.S. Census Bureau County Business Patterns data, health services increased from 11.1 percent of City employment in 1980 to 15.2 percent in 1990, and from 10.3 percent of City payroll in 1980 to 16.2 percent in 1990. In addition, health services makes up a larger portion of the region's economy than is the case in many other major metropolitan areas, which suggests that the region has some unique locational advantages from which the City has benefited, and may continue to benefit. However, the possibility of Federal health care reform, combined with the ongoing reality of restructuring in the health care industry, poses risks to employment in this sector.

- o Hospitality sector growth. Investments in the Pennsylvania Convention Center, the Avenue of the Arts and the Delaware Avenue waterfront area are likely to create a substantial number of jobs in hospitality industries. This will continue the trend of the conversion of the City's economy from manufacturing to services, and also place significant new emphasis on certain elements of the service sector. Some of the industries which are likely to benefit include eating and drinking places, hotels and lodging places, museums and amusement and recreation services. The average 1990 wage for these sectors, based on U. S. Census Bureau County Business Patterns data, is $11,859, compared to an average for all jobs of $25,393. While the actual average earnings of jobs created may be higher, and any new jobs are welcome, the average wage of jobs created seems likely to be lower than the City average, and likely to not have as large an impact on tax revenues as new jobs in other industries.

A PICA Staff analysis, prepared in connection with its review of the Plan, projected the impact on average wage per employee growth if it is assumed that wages for all sectors grow at the Plan-projected rate of 4 percent annually, and job growth continues as projected in the Plan, but that the employment distribution continues to change as it has since 1983. The analysis produced a projected reduction in the *share* of jobs in manufacturing by 3.8 percent, a reduction in transportation and public utilities by 1 percent, wholesale trade by 1.1 percent and retail trade by 0.5 percent. Government increased by .4 percent and services by 6.4 percent. These changes, when applied, suggest cumulative Wage Tax revenues of $50 million less than the Plan anticipates through FY99.

Suburban Withholding -- *Prospects are still speculative*

The City, appropriately, has not assumed the enactment of suburban withholding legislation in Plan revenue estimates. Under such legislation, non-Philadelphia employers would be obligated to withhold Wage, PICA and Earnings Taxes on the compensation Philadelphia residents. The legislation was passed by the State Senate in April 1993, but remains in committee in the House of Representatives. The City initially estimated an eventual $9 million annual impact from suburban withholding legislation.

In lieu of suburban withholding legislation, the City had proposed working with suburban tax administrators to encourage businesses to withhold taxes from Philadelphia residents at local earned income tax rates and remit such withholdings to the City as a portion of the employees' liability. This proposal has been abandoned.

The City continues to match U.S. Internal Revenue Service shared data to its internal tax data base and, additionally, plans to track residents by suburban employer and offer *en-masse* settlements in exchange for employer agreement to voluntarily withhold and remit Wage Taxes.

Real Estate Tax -- *The projections assume a recovery in the commercial, industrial and residential real estate markets*

Real Estate Tax projections for FY94 have been reduced from $369.3 million in the FY94-FY98 Plan to $336.1 million in the January Monthly Mangers Report, a reduction of 9.0 percent. The same figure is used in the Plan. Current Real Estate Taxes were $303.9 million in FY93, and are projected to be $307.6 million in FY94, a growth rate of 1.2 percent. FY94 collections through the end of March were $284.0 million, 1.6 percent below collections for the same period in FY93. Although Real Estate Tax collections are not always distributed similarly over the fiscal year, this is cause for some concern about whether the City will meet even its recently-lowered Real Estate Tax projection.

Prior Real Estate Tax collections were $26.6 million in FY93, and are projected at $28.5 million in FY94, an increase of 7 percent. However, FY94 prior Real Estate Tax collections are $19.0 million through March, 1994, a 0.4 percent decrease from the same period in FY93. This too is a cause for concern. Totals suggest that the impact of collections initiatives in the Revenue and Law Departments may be beginning to diminish, although some of the Revenue Department's computerization initiatives may be helpful.

The projection for current Real Estate Tax revenues relies upon assumptions based on four key factors: (1) projected increases in taxable assessed value due to abated properties returning to taxable status; (2) increases in assessed value due to growth in market values; (3) reductions in assessments due to appeals; and (4) collection rates of current and prior year taxes. The projection assumes that all returning abatements are commercial/industrial properties, and growth in both the residential and commercial/industrial portions of the assessment base.

The projection for abatements returning to taxable rolls is known with some certainty for the next three years, since any new construction within the that period will not be taxable until the fourth or fifth year of the Plan. The value of abated property returning to taxable status is projected to decline significantly from the level of the past three years, as the impact of the Center City office building boom of the 1980's passes. Abatements returning were $124 million in assessed value in FY92, $149 million in FY93 and $259 million in FY94. This figure is projected to drop to around $60 million in both FY95 and FY96, and $10 million in FY97. Any additional returned abatement amounts in later years will be due to new construction, and are assumed to be considerably less than recent figures.

The growth in the underlying tax base -- the growth in assessed value after appeals in one year to certified assessed value prior to appeals in the following year -- is estimated at 1.2 percent in FY92, 0.3 percent in FY93, and a negative 0.9 percent in FY94. Growth in base assessments in the residential sector is projected at 1.5 percent in FY95, and 2 percent in FY96-FY99. In the commercial/industrial sector, assessment base growth is projected at a negative 0.25 percent in FY95, 0.6 percent in FY96, and 1 percent in FY97-FY99. The separate residential and commercial/industrial growth rates combine into an effective growth rate for the total tax base of 0.8 percent in FY95, 2.2 percent in FY96, 2.3 percent in FY97 and 2.2 percent in FY98-FY99. Given the decline in FY94, the projected positive growth in FY95 and after is an upturn from recent trends. The projected growth rates are modest enough that they appear reasonable, but nonetheless depend on a recovery in the real estate market. This may be justified, given that residential real estate values appear to be stabilizing following declines of the early 1990's. With respect to the commercial real estate market, however, the projected recovery appears further off. One of the factors that may delay a recovery in the commercial market is the continuing decline in employment projected through FY99 in the Plan. Absent a stabilization of employment in the City, it is unlikely that demand will be adequate to cause a significant increase in assessed values.

The negative impact of reduced levels of returning abatements will be compensated for to some degree by moderation in the expected level of reduction in assessments due to appeals. Reductions in assessments due to appeals were $172 million in FY93, dropped to $84 million in FY94, and are projected to drop to $64 million FY95 and FY96, $56 million in FY97, $52 million in FY98 and $48.5 million in FY99.

The projection of prior Real Estate Tax revenues is for level collections throughout the Plan. Based on trends in prior collections as a percent of total revenues, this projection appears aggressive. The decline between FY93 and FY94 prior collections for the first nine months of the current fiscal year is also cause for concern.

Business Privilege Tax -- ***The volatile nature of this tax makes it difficult to project on the basis of historical trends***

The City projects Business Privilege Tax (BPT) revenues at $225.9 million in FY94, up 5 percent from FY93. Collections through March are running 31 percent above the same period in FY93, which suggests the City will meet its revenue target for the BPT this year. However, an accurate assessment of each fiscal year's collections is not possible until after April, when the bulk of collections are received. As a result, the high rate of collections to date may not reflect the final outcome. However, preliminary surveys by the City Controller's Office of business profits and receipts indicate that the FY94 estimate is on target.

The City has based its Plan projections on its assessment of the historical trend, plus an adjustment to reflect the additional collections due to revenue initiatives. However, given the volatile nature and relatively short history of this tax, it is difficult to determine an historical trend. BPT collections grew at a 1.6 percent annual rate from FY89 to FY93. They also grew at a 5.6 percent annual rate from FY88 to FY93. The difference is due to the large increase from FY88 to FY89 of 21.7 percent, which was due in part to a rate change. The historical growth rate for this tax is very sensitive to the choice of historical periods over which it is measured. Its volatility could be explained by its sensitivity to performance to a few industries and large firms, due in part to the fact that many companies are totally or partially exempt.

The Plan states that BPT collections grew 2.9 percent over the last five years, after adjusting for rate changes. Adjusting for rate changes is not a simple matter for the BPT, given its provision allowing some industries to choose between the lesser of the gross receipts portion and the net income portion of the tax, and other provisions that allow some industries to use alternate bases and rates for the gross receipts portion of the tax. Even if the effects of the rate change in FY88 could be factored out, the growth from FY87 to FY88 was apparently much larger than any year since. As a result, it is not clear whether FY88 properly should be part of a calculation of the trend.

Even if one accepts the trend at 2.9 percent, the Plan's BPT projection is considerably higher -- 3.7 percent. The Plan indicates the increase from 2.9 percent to 3.7 percent is entirely due to improved enforcement. This cannot be due to improved collections of prior taxes, since prior collections are projected as flat through the term of the Plan. If the additional revenues are current collections, there will be an additional 0.8 percent in annual growth, or $1.5 million, in current BPT collections. This is higher than the revenue projected for the automated audit system, and will be a challenging target to hit.

As well, there is the same problem with prior collections of BPT as for the other taxes. The prior collections projection could be aggressive based on the trend in prior collections as a percent of total collections.

Sales Tax -- *Monthly collections have been stabilizing, and the projection appears to be reasonable*

FY94 Sales Tax revenues through March are 11.4 percent above the same period in FY93. The FY94 projection is for $82 million, a 7.5 percent increase over FY93. Monthly tax collections are steady, generally running at approximately $7 million per month.

Based on the Monthly Revenue Report from the Commonwealth, Sales Tax collections statewide increased 4.3 percent in the first seven months of FY94 over the same period in FY93. The reason for the City's relatively large increase compared to the State appears to be an improvement in the State's collection system for the local Sales Tax. If Philadelphia's underlying Sales Tax base increases at the same rate as the State's, 7.1 percentage points of the revenue increase in the City through March are due to improved State collections. As collections improvements become integrated into the system, it should be possible to determine what the growth in the underlying base actually is, which will assist in making accurate projections.

The Plan projects Sales Tax revenues to increase 4 percent in FY95, and 3.5 percent in FY96-FY99. The increase in FY95 is justified as the likely impact of sales increases and continued improvements in the State's collection system. In FY96-FY99, the projected increases are equal to inflation, and assume no further improvements in the State's collection system. Since the City's projections for underlying growth in the Tax base, 3.5 percent annually in each year of the Plan, are below the State's current level of growth in Sales Tax collections, the City's projection appears reasonable.

The City received a one-time payment in November of 1993 for Sales Tax associated with sales by State Liquor Stores located in Philadelphia. This payment covered taxes paid for purchases back to October 1991. After November, revenues from liquor store sales have been included in the monthly receipts. As a result, the calculation of growth from FY93 to FY94 will be slightly inaccurate unless revenues from liquor store sales are apportioned to the appropriate fiscal year. The City indicates that the $1 million in liquor store sales has been taken out of the Sales Tax's base in the Plan (FY94).

Real Estate Transfer Tax -- *The Plan's projection could be aggressive since the tax base is assumed to grow more rapidly than the real estate market overall*

The Real Estate Transfer Tax (RETT) projection could be aggressive since it is assumed that some sales will be postponed to take advantage of lower transfer tax rates in FY94 and FY95. The RETT rate was 3.45 percent in FY93, is 3.23 percent in FY94 and will be 3 percent in FY95 and thereafter. Based on these rates and projected revenues, the assumed growth in the base for the tax is 6 percent in FY94, 3.8 percent in FY95 and 3.5 percent in FY96-FY99.

There does not appear to be any correlation between the Real Estate Tax projection and that for the RETT. The projected growth in the RETT tax base is larger than the projected growth in the Real Estate Tax base. This could, however, be accounted for by assuming that the number of sales increases due to the stabilization of the market, even if values do not increase. The projected growth in FY94 and FY95, particularly, could be aggressive in light of the high assumed growth rates in the base of the tax in those years and still-weak local conditions.

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DEBT

Primary Areas of PICA Concern
o FY95 Short-Term Interest Estimates
o New Bond Issues

Plan Expenditure Projections FY95-FY99 (millions)

	FY95	FY95-FY99
Long-Term Leases	$38.2	$195.1
Interest Long-Term Debt	41.6	257.7
Principal Long-Term Debt	44.7	208.3
Interest Short-Term Debt	14.9	74.6
Sinking Fund Reserve	9.7	21.7
Commitment Fees	4.5	22.5
Arbitrage Rebate	0.8	0.8
Total	$154.4	$780.7

Introduction

The City's debt service and long-term lease payments are estimated at $140.0 million in FY94, and are projected to be $154.4 million in FY95, $149.6 million in FY96, $152.9 million in FY97, $158.9 million in FY98 and $165.0 million in FY99. This is a significant reduction from FY94-FY98 Plan levels. The total of the current FY94 estimate and currently projected FY95 to FY98 levels in the FY95-FY99 Plan is $123.6 million less than the sum total of projections for the same period in the FY94-FY98 Plan. This reduction in debt service costs reflects the favorable impact of the debt refinancings that took place in the summer of 1993. The cited cost reduction is not a "net" saving, since PICA debt service increased as a result of the refinancings, which in turn reduces City revenues. The estimated net savings over the FY94-FY99 period from the 1993 refinancings (both directly by the City and through PICA) is $43.4 million. Of these savings, $16.4 million occurs in FY94.

There may be an opportunity for additional refunding savings if the City regains its investment grade ratings or has access to credit enhancement. No such savings, however, appear to have been assumed in the Plan.

Short-Term Debt Interest -- *The Plan budgeted amount appears overly generous, given the projected repayment schedule*

The FY95-FY99 Plan's estimates of interest on short-term debt and the cost of issuance of short-term debt are significantly higher than either FY94 budgeted or estimated levels. The short-term debt interest estimate is based on an assumed $390 million loan at an interest rate of 4.17 percent for eleven months. FY95 cash flow projections anticipate that notes will be issued in July 1994 and repaid during the months March, April and May 1995, the principal amount thus being outstanding for less than a full 11-month period. The current estimate for FY94 costs includes a $350 million loan at the same interest rate for a nine month period. The cash flow projections for both FY94 and FY95 contemplate similar timetables for repayment. Thus, even taking into account the prospect of higher interest rates in FY95 than in FY94, there appears to be a cushion in the FY95 short-term debt interest estimate of about $2 million.

In the version of the FY95-FY99 Plan approved by City Council, loan commitment fee expenses were increased to $4.5 million in each year of the Plan, compared to $3.5 million in the original version of the Plan. These amounts are significantly larger than both the estimated FY94 level of $3.6 million and the FY94 budget figure of $2.5 million.

New Bond Issues -- *City debt service estimates appear high, given that some of the originally assumed costs of a City FY95 issue will be reduced by a contemplated FY95 PICA borrowing*

The Plan states that the City hopes to achieve an investment grade bond rating in calendar 1994, which might allow a City general obligation bond issue in FY95. The original FY95-FY99 Plan debt service projections assumed that new general obligation City debt would be issued in each fiscal year of the Plan. The assumption was that $125 million in debt would be issued each year at an 8 percent interest rate. The additional interest and principal expenditures resulting from these issues were originally projected to be $11.5 million in FY95, increasing to $55.7 million in FY99.

In the version of the Plan approved by City Council, $90 million of the original $125 million new City issue in FY95 is now anticipated to be issued by PICA, and obligations for City debt service were reduced, while PICA debt service expenditures were increased (reflected as a reduction in PICA Tax revenues for the City). The Plan increased FY95 capital projects to $145.5 million. The FY95-FY99 Plan as originally constructed included debt service payments for the proposed PICA issue as City debt service payments. Such payments are required to be made by the Authority, and PICA debt service costs accordingly are offset against PICA Tax revenues prior to remitting those revenues to the City. Debt service on PICA bond issues is paid from the PICA Tax, which is a tax on the wages, earnings, and net profits of City residents dedicated to the Authority's bondholders. Absent continuance of an uncorrected variance in a five-year financial plan, PICA Tax revenues remaining after PICA debt service is paid are transferred to the City from the PICA City Account.

In the version of the Plan approved by City Council, changes were made to offset debt service costs related to the anticipated FY95 PICA issue against revenues anticipated to be received by the City from the PICA City Account, and to reduce City anticipated debt service costs to recognize only the costs of projected FY95 City general obligation borrowing. The effect of the changes was to reduce City long-term debt service by $37.5 million over the life of the Plan, and increase PICA debt service costs (decreased City revenues from PICA taxes) by $30.8 million.

PICA Staff analysis of a hypothetical debt service schedule provided to PICA by the City for the proposed FY95 PICA and City issues indicates discrepancies between the new City debt service projections and the changes which were made in the Plan to recognize the changes in such debt service projections. PICA Staff analysis indicates that the long-term debt interest provision should have been reduced an additional $6.8 million from revised Plan levels and long-term debt principal payments increased by $1.3 million over the revised amount. The net impact on long-term debt service (the variance between City supporting documents and the City Council-approved Plan) is anticipated expenditures in excess of apparent needs to service new City long-term debt of approximately $25 million of $5.5 million. Adjustments made to PICA debt service in the revised Plan appear to be appropriate.

It is reasonable to include new issue cost estimates in the Plan, but they are only estimates. The City and PICA will jointly review capital projects proposed to be funded through PICA funding to determine whether the projects fit the criteria stated in the PICA Act (that capital projects to be funded by PICA are emergency in nature, or designed to increase revenues, reduce expenditures, or enhance productivity).

Under the PICA Act, the Authority is permitted to issue its bonds (other than refunding issues) only through December 31, 1994. Given PICA's investment grade ratings, and the likelihood of any upgrade of the City's rating also being productive of an improvement in the Authority's rating, it is reasonable to assume that PICA will commit substantially all of its remaining borrowing capacity prior to the end of the year. Under its bond indenture the Authority is required to show historic debt service coverage (in the form of PICA Tax revenue) of at least $1.75 for each dollar of debt service for a 12-month period in the 15 months preceding the date of issuance, and similarly, prospective coverage, which may be based on the PICA Tax projected to be collected in the City's most recent PICA-approved Plan, of $1.75 for each dollar of debt service during the 12 months following the issuance of additional bonds. The corrections made by the City to the manner in which the City collects the PICA Tax increases the amount of revenue available for PICA debt service, and the Authority has begun the work necessary to assess its total borrowing capacity.

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PERSONNEL

Primary Areas of PICA Concern

- No Projected Change in Personnel Complement After FY95
- No Wage Increases in FY97-FY99
- Health Benefits Growth Rate
- Pension Payments

Plan Expenditure Projections
FY95-FY99
(millions)

	FY95	FY95-FY99
Personal Services	$ 876.1	$4,498.0
Fringe Benefits	447.9	2,512.5
Total	$1,324.0	$7,010.5

Introduction

Significant savings have been achieved since FY92 in the City's spending for wages and benefits, made possible by reductions in personnel levels, as well as savings achieved in the cost of salaries and fringe benefits. The FY95-FY99 Plan projects cost growth, however, with personnel levels projected to increase somewhat, and health benefits projected to increase at 12 percent annually (producing FY99 health benefits costs 82.7 percent higher than actual FY93 expenditures). No changes in wages are anticipated in the last three years of the Plan, which is an aggressive assumption, but understandable in light of negotiations which will be aimed at yielding new labor agreements in July 1996. As a result of this assumption, Class 100 cost increases are below the rate of increase of tax revenues (including the PICA Tax) in the last two years of the Plan, FY98 and FY99. Class 100 costs are above tax growth by 0.3 percentage points in FY96 and 0.7 percentage points in FY97, but below by 0.7 percentage points in FY98 and 0.6 percentage points in FY99. Achieving structural balance depends in part on fairly aggressive assumptions concerning salary growth, or a moderation in the rate of growth of health care benefits.

The Plan projects few significant changes to personnel policies beyond the implementation of disability reforms and work practice changes permitted by the collective bargaining agreements. The acceleration of personnel cost growth in each year of the Plan, well in excess of tax revenue growth, demonstrates the absence of structural balance in the City's budget, and is driven by dramatic projected growth in health care benefits. Particularly if wage increases are granted at any time in the last three years of the Plan, further personnel efficiencies will be needed to maintain Plan balance.

Projected Personnel Levels -- ***The Plan projects no significant changes in staffing levels after FY95***

As was the case with PICA Staff's review of the FY94-FY98 Plan, a major concern for this Plan is the fact that significant staffing changes are projected in the first year of the Plan, but no significant changes are projected thereafter for almost all departments. The current FY94 year-end projected General Fund staffing level is 23,413, while the projected FY95 level includes 23,941 positions. This increase of 528 positions is mostly attributable to increases of 87 positions in the Fire Department, 67 in Human Services, 14 in Licenses and Inspections, 220 in Police, 160 in Prisons, 47 in Public Health and 14 in Recreation. These increases are offset to some extent by a decrease of 24 personnel Civic Center and 32 in Streets and the transfer of 55 Fleet Management positions from the General Fund to the Water Fund. After FY95, except for small reductions in staffing at the Atwater Kent Museum and the Betsy Ross House and additions to DHS complement, there are no staffing changes projected in the Plan.

It is disappointing that the Plan does not attempt to account for likely changes in the City's priorities and staffing levels over the full five years of the Plan. The development of a strategic plan for the City should assist in making the Plan a more realistic statement of the fiscal impact of the City's priorities, but the Plan evidences no fiscal impact of substantive changes in the way the City does business. It seems likely that additional staffing will be desired or required in some organizations that will have to be accompanied by reductions in other areas to maintain Plan balance, and there is no effect included in the Plan for additional benefits from new competitive contracting efforts. These changes do not appear to have been considered as part of the Plan process. As a result of the Plan's personnel assumptions, any increases in overall General Fund personnel levels, or any increase in the average wage of General Fund employees as a result of changing the distribution of employment among departments, will result in an imbalance in the Plan, absent compensating adjustments elsewhere.

Salary Projections -- ***The Plan assumes no increase in salaries after the scheduled increases of 2 percent in FY95 and 3 percent in FY96 take effect***

The Class 100 expenditure projections for most departments appear to reflect only the known impact of salary changes that will occur in FY95 and FY96 as a result of labor contracts currently in force. Based on these contracts, uniformed Police and Fire employees will receive a 2 percent wage increase effective January 1, 1995, and a 3 percent increase effective January 1, 1996. Non-uniformed employees represented by D.C. 33 and D.C. 47 will receive wage increases of 2 percent effective April 1, 1995 and 3 percent effective April 1, 1996. These increases are taken into account in the Plan. No further wage increases in FY97, FY98 or FY99 are projected in the Plan. While it is possible that no wage increase will be provided in these three years, PICA

Staff is concerned about whether salary increases will be needed to maintain competitiveness with other employers, or whether salary increases will be unavoidable due to arbitration.

PICA Staff has a related concern with the use of inconsistent methodology by departments in preparing their FY95 Class 100 budget, upon which subsequent Class 100 projections in the Plan are based. Some departments budget explicitly for a 2 percent salary increase in FY95, while others do not. This raises a concern about the methodology used in calculating these increases, and central administration should pay more attention to requiring a consistent approach.

FY95 Staffing and Class 100 Expenditures -- *An increase in staffing is projected without a significant increase in expenditures*

Total Class 100 expenditures are projected to increase only 0.22 percent in FY95 from their FY94 estimated level. At the same time there are increases in overall personnel levels in some departments. The Fire Department had 2,306 filled positions as of March 20, 1994, is projected to be at 2,330 at year-end FY94, and is budgeted at 2,417 in FY95. Fire Department FY95 budgeted personal services expenditures increase only 2.8 percent over FY94 estimated levels. The Police Department staffing level is at 6,930 as of March 20, 1994, is projected to be at 6,887 as of year-end FY94 and is budgeted at 7,097 in FY95. Police FY95 budgeted expenditures in Class 100 increase only 0.5 percent over FY94 estimates. The Prisons' Department personnel level is 1,820 as of March 20, 1994, is projected to be at 1,890 as of the end of FY94 and is budgeted at 2,050 in FY95. Prisons' FY95 budgeted expenditures increase 5.6 percent over FY94 estimated levels. Overall, General Fund personnel levels were at 22,934 as of March 20, 1994, are projected to be at 23,413 by the end of FY94 and are budgeted at 23,941 in FY95, a 4.4 percent increase over March 20, 1994 and only 124 fewer employees than the City had on June 28, 1992.

Reaching these staffing goals within budget targets largely depends on assumptions about the impact of two initiatives: civilianization and lower starting salaries in both the Police and Fire Departments. The Police and Prisons Departments have stated their intention to replace higher-paid uniformed employees with lower-paid civilian employees in the same jobs. The City has noted that the Prisons Department civilianization program's success is contingent on renegotiating the existing consent decree which mandates correction officer staffing levels. The reduction in starting salaries for uniformed employees in the Police and Fire Departments was granted in the most recent Act 111 arbitration awards, and the impact of this initiative on departmental salary costs will depend to a large extent on attrition and future hiring. The City's ability to attain desired staffing levels in the Police, Fire and Prisons Departments, given the small projected increase in departmental Class 100 expenditures in FY95, will require that new policies are implemented as planned. Since the out-years of the Plan are based on the assumption that FY95 staffing and budgetary targets are consistent, maintaining projected personnel levels in the out-years will also require successful implementation of these initiatives.

Health Benefits -- ***The projection of a 12 percent annual increase is warranted given projected increases in personnel levels and the 11.7 percent increase in per employee rates in FY94***

There are two factors that affect the City's health benefits costs in a fiscal year: the monthly per employee contribution and the monthly number of employees on the payroll. City costs for health benefits decreased 17.8 percent in FY93 due to new collective bargaining agreements and increased only 3.1 percent in FY94. The annual City contribution increases in FY94 for the City's non-uniformed unions were 11.7 percent, based on the standard negotiated in the contracts for increases equal to the average annual increase of the three largest HMOs in the Philadelphia region. However, the total FY94 increase was greater than otherwise would have been the case since a reduction in the Police health benefits contribution was not implemented for all of FY93, and a reduction in the Fire health benefits contribution was not implemented until FY94.

The rate of growth in the cost of health benefits in FY93 and FY94 was extremely favorable compared to past trends, due to the combination of reductions in the cost per employee per month and the number of General Fund employees. Future trends, in FY95 and after, for both employment and cost per employee are not anticipated to be as favorable.

In its most recent round of contract settlements, the City achieved significant reductions in its monthly per employee cost of benefits. As a result of these settlements, the monthly per employee cost of health benefits for employees of D.C. 33 decreased from $482 to $360 effective at the beginning of FY93; the cost for employees of D.C. 47 decreased from $437 to $360, effective at the beginning of FY93; the costs for uniformed Police employees decreased from $483 or $490 to $400, effective April 1, 1993; and the cost for uniformed Fire employees decreased from between $508 and $562 to $450, effective November 30, 1993. These reductions have had a major positive effect on health benefits costs in FY93 and FY94.

Personnel levels also had a positive impact on health benefits costs in FY93 and FY94. Between FY92 and FY93, full-time General Fund personnel levels declined significantly. Although the number of filled General Fund positions is projected to be higher at year-end FY94 than at year-end FY93, the average monthly employee level in FY94 may actually be slightly lower than in FY93. This is because of the high employee levels in the early portion of FY93, and employee levels though most of FY94 that were only slightly above year-end FY93 levels. The decline in average personnel level would have a positive effect on trends in health benefits costs between

FY93 and FY94, although projections as to future employment levels give little reason to expect similar declines in the future.

Health benefit cost increases in the future could be considerably larger since these moderating factors will be no longer present. However, some of the impact of the recent contract settlements should carry over into FY95, since the post-contract Fire cost per employee per month will be in effect for all twelve months of FY95 instead of eight months, as was the case in FY94. Under the current contracts, the cost per employee per month will increase at the rate of the average of the three largest HMOs in the Philadelphia region. This formula resulted in an increase in the City's per employee health benefit costs of 11.7 percent in FY94. Average employment in FY95 is likely to increase over FY94 levels, and under Plan projections, average employment is expected to remain constant after FY95.

The Plan assumes 12.7 percent growth in health care benefit costs in FY95, and 12 percent annual growth in FY96-FY99. These assumptions appear reasonable, but could be high, since the prospect of some type of national health care reform, combined with ongoing restructuring within the health care industry, may slow the rate of growth in costs over the next few years. However, the City should not budget on the basis of an assumed national health care plan. As long as rates for the region's HMOs continue to increase at levels near 12 percent, as they did in FY94, an assumption of 12 percent annual growth throughout the Plan is appropriate. The slightly higher growth assumption of 12.7 percent in FY95 is also reasonable in light of the anticipated increase in costs per employee as well as in the average monthly number of full-time employees. The likelihood of employees being added over the course of the 1995 fiscal year makes it likely that the 12 percent figure may be somewhat conservative.

Other Benefits -- *Legal benefits appear likely to increase, but no increase is contemplated in the Plan*

Group legal benefits were $10 per month per non-uniformed employee in FY94, and under the settlement with the non-uniformed unions, will increase to $12 per month per employee in FY95. Legal benefit levels for Police will remain at $20 per month per officer in FY95 and Firefighters will continue to receive $16 per month. The Plan budgets no increase for group legal insurance to reflect the increase in non-uniformed payment levels or the projected increase in Police and Fire staffing, so this figure could be under budgeted by approximately $500,000.

Projections for FICA costs appear reasonable since they increase at rates slightly above the projection of growth in overall Class 100 salary expenditures.

"Flex cash" payments are projected to remain constant over the Plan, which is of some concern since, while not tied to the cost of medical benefits, these payments are made to non-unionized employees to provide choice in health benefit selection, and could thus be expected to grow at the projected rate of other health care benefits, which is 12 percent.

Disability costs decline significantly over the Plan, which is the projected result of efforts being undertaken by the City's newly-established Risk Management Division. These efforts are discussed in a separate section of this report, as are the attendant risks.

Overtime -- *Budgeted reductions will not be achieved in FY94*

Overtime costs declined from $62.4 million in FY92 to $56 million in FY93, and were projected in the Monthly City Managers Report for February 1994 to total $57.2 million in FY94. However, the Managers Report's FY94 projection is a significant (29.4 percent) increase from the adopted budget level of $44.2 million, in part the result of severe winter storms in January. Nonetheless, FY94 overtime expenditures are still likely to be well below the FY92 level, which is a remarkable achievement given the substantially lower number of City employees in FY94 compared to FY92. The City includes a contingency for unexpected events such as severe winter weather in its overtime budget, and it is reasonable to plan for at least one unexpected event annually with an overtime impact comparable to that of this year's winter storms.

Pension Payments -- *The Plan does not explicitly anticipate either interest costs or a potential settlement with the Auditor General*

Pension costs grew 15.7 percent from FY90 to FY91 and 25.9 percent from FY91 to FY92, declined 0.5 percent from FY92 to FY93 and are estimated to increase 5.3 percent from FY93 to FY94. The increase in FY94 includes the impact of an estimated $4.5 million in interest to be paid, at a 9 percent rate, on amounts due at the beginning of the fiscal year but paid later in that year. The Plan includes minimal payment increases in FY95 and FY96, and 5 percent annual increases in the later years. The projections in the FY95-FY99 Plan are significantly lower than those in the FY94-FY98 Plan ($26.7 million over the FY95-FY98 period). The differences between the two Plans are primarily due to a significantly lower growth rate in FY95 and FY96 in the FY95-FY99 Plan. FY95's projected growth in the FY94-FY98 Plan was 1.9 percent, compared to zero percent growth in the proposed FY95-FY99 Plan; FY96 growth was 2.5 percent in the FY94-FY98 Plan, compared to 0.7 percent growth in the proposed FY95-FY99 Plan.

In previous reports, PICA Staff described its concerns that certain factors were not taken into account by the actuarial analysis on which the projection of pension costs in the FY94-FY98 Plan was based. The FY94-FY98 pension contributions contained in the original FY94-98 Plan were reduced from the Mayor's proposal to the final

FY94-FY98 Plan approved by Council based on an analysis by a consulting actuary that took into account lower salaries and certain disability plan changes. PICA Staff previously has stated its concerns that the analysis did not account for changes in the number of personnel employed by the City, the potential impact of other disability system reforms, the potential for changes in fund earnings in light of declining interest rates and the condition of the real estate market, stock prices and dividends. PICA Staff has seen an analysis taking into account only some of these additional factors. The lack of such a complete analysis is of particular concern since pension cost projections in the FY95-FY99 Plan are significantly lower than the final FY94-FY98 Plan levels.

As noted in previous PICA Staff Reports, the State Auditor General has determined that the City owes the State $18 million as a result of the City's alleged underfunding of its pension obligations in fiscal years 1988, 1989 and 1990. The City has contested some of the findings of the Auditor General, contends that it has overpaid for the years in question, and has noted that other of the practices cited by the Auditor General have been corrected. The City has proposed that an actuary study the impact of the City's alleged noncompliance with applicable regulations concerning the pension fund and has proposed that any adverse impact be funded by the City on a multi-year basis. The City is still in negotiations with the Auditor General regarding the appropriate way to address the issues identified. Any additional funding that will be required as a result of this matter will have an adverse impact on the Plan, since no specific funding is included to cover any costs resulting from an such agreement. Funding for any settlement will have to be made up through savings in other parts of the Plan.

Another area of cost that has not been specifically included in the Plan is the pension interest costs that are currently estimated at $4.5 million in FY94. The City has a reason for not specifically budgeting for this cost. State law requires that the City pay into its pension fund the minimum municipal obligation (MMO) determined by an actuarial valuation or the amount the City budgets as a payment to the pension fund, whichever is larger. As a result, the City budgets only the MMO amount although it may need to pay additional interest costs on amounts due at the beginning of the fiscal year but not paid until later in the fiscal year. This ensures that the City is not forced to pay a larger amount than is needed to contribute the MMO plus appropriate additional interest costs. The FY95 budget and the FY95-FY99 Plan do not contain funds for interest replacement costs. These amounts will have to be made up through savings achieved in other parts of the Plan. PICA Staff is concerned that the City is incurring unnecessary interest costs in making payments to the Pension Fund over time, and notes that the City's cash flow position is now such that it should consider making the full payment when it is due.

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RISK MANAGEMENT/INDEMNITIES

Primary Areas of PICA Concern

- o Employee Disability System Reforms
- o Backlog in Worker's Compensation Cases
- o Future CSI Contract Costs
- o Potential Risk Areas in the Indemnity Budget

Plan Expenditure Projections FY95-FY99 (millions)

	FY95	FY95-FY99
Risk Management	$ 1.4	$ 7.5
Indemnities	21.0	141.3
Total	$22.4	$148.8

Introduction

The Division of Risk Management is situated within the Office of the Director of Finance and has four organizational units: Claims; Risk Management; Employee Disability; and Safety.

The Claims Unit, formerly housed in the Law Department, manages, settles, or closes claims against the City prior to litigation. The Unit investigates incidents that could lead to claims; processes claims, and enforces the City's subrogation rights to seek recovery from third parties for damage to City property. Subrogation recovery was contracted out from November 1992 to November 1993, but was moved in-house after the contract expired.

The Risk Management Unit directs the Division and analyzes City risk exposure issues. The Unit is currently evaluating the City's reliance on purchased insurance coverage and self-insurance, and is working to identify specific risks and potential losses to determine where safety mechanisms are needed. According to the Division, the savings from this effort are expected to be realized over the long-term as the City's net insurance and claims costs decline. To aid in this effort, the City is developing a database of information relating to past claims and injury incidents. Based on information currently maintained by individual departments, records relating to past injuries and claims and their costs will be compiled and computerized. The information will assist in quantifying risk areas where benefits may be achieved through additional safety measures. This database will also provide a baseline against which to measure the City's progress in reducing risks and costs.

The Safety Unit has begun programs designed to improve the work environment for City employees and prevent injuries to both City employees and third parties. The Unit implements safety requirements that are mandated for all self-insured employers by the Pennsylvania Workers' Compensation Act.

The Employee Disability Unit manages the Employee Work-Related Disability Program for City employees. A number of reforms in the Workers' Compensation/Injured-On-Duty Program (WC/IOD Program) system have been completed, or are in the process of being implemented. These reforms were designed, in part, to reduce the City's rapidly increasing costs for employee disability.

Employee Disability System -- ***Major reforms are being instituted, and the Plan depends on their successful implementation***

Through contract negotiations and arbitrations with the City's four major municipal unions, the following changes have been made to the City's employee disability system: "double dipping" (the practice of collecting both a City disability pension and workers' compensation) was eliminated for employees disabled in the future; earned income offsets were instituted, where City ordinary or service-related disability pensions are reduced by between 33 and 50 percent of the amount of earned income of the pension recipient; more generous benefits were instituted for totally disabled employees; and injured-on-duty pay, which is tax-free, was reduced from 100 percent to 75 percent of base salary for employees required by law to pay social security and 80 percent of base salary for employees who are not required by law to pay social security.

Another recent initiative is the negotiation of a contract with CompServices Inc. (CSI), a subsidiary of Independence Blue Cross, to provide required medical care, claims investigation, medical and claims management, information management and vocational rehabilitation services for all City employees injured on the job. The contract became effective January 1, 1994. The cost of the contract is based on a capped fixed price relating to the monthly number of active employees. The capped cost provision requires CSI to pay the lower of either 113 percent of the Medicare rate, or the Blue Cross rate of 53 percent of retail. As a result of the CSI contract, savings are expected from reduced average injury time and reduced fraud and abuse, while the City expects quality of care to improve.

Philadelphia City employees who are injured on duty have the option to receive wage replacement benefits under the Pennsylvania workers' compensation system or under the City's Regulation 32 system for temporary injuries. Employees who are permanently disabled can receive wage replacement through workers' compensation or a service-connected disability. Regardless of which option they choose, they now will receive medical services under the CSI contract. The Plan states that the City hopes that an increasing number of employees will choose the Regulation 32 option for wage replacement, because the City will retain greater control over treatment, the treatment will be cost less due to fixed price arrangements and in-house treatment increases the chance that employees will return to work more quickly. The incentives the City has provided to encourage employees to choose the Regulation 32 option are that under Regulation 32, wage replacement payments are 75 percent or 80 percent of base salary, compared to 66 2/3 percent offered under workers' compensation. Also, under Regulation 32, employees continue to receive medical benefit coverage and accrue sick leave time. Wage replacement under Regulation 32 is paid directly from departmental budgets, through the payroll system. Workers' compensation wage replacement is funded by the Department of Finance and administered through the CSI program.

CSI is also responsible for performing subrogation work related to employees who are injured on duty. The principle of subrogation grants the City rights under the Pennsylvania Workers' Compensation Act to receive reimbursement for medical expenses and wage-loss payments if an employee with a work-related injury obtains a recovery against a third party, or to pursue reimbursement directly from the third party if the injured employee chooses not to litigate.

The City is projecting a large reduction in disability-related costs in the Plan as a result of these changes. The reduction is based on a number of assumptions, and if any of the assumptions are not realized, disability expenditures could be greater than projected in the Plan. The lack of a track record and the as-yet uncompiled past history of the City make such assumptions tenuous, but not necessarily unreasonable.

Workers' Compensation -- *A dramatic turnaround from past cost trends is projected and the present backlog is to be reduced*

Workers' compensation costs are projected to decline from $31.5 million in FY94, to $25 million in FY95 and by $1 million annually thereafter through FY99 to $21 million. The reduction in FY95 results in part from transferring medical costs to the CSI line item. Effective January 1, 1994, all medical care under workers' compensation is either delivered or paid for under the CSI contract. The remaining reduction in workers' compensation costs in FY95 is to be derived from four factors: aggressive litigation management; adjusting medical evaluation techniques to limit liability; consistent internal application of City policy and procedure; and a secondary employment program. The secondary employment program will develop plans for re-employment and rehabilitation for employees who are permanently disabled from their City job but wish to continue to work within City government.

In view of recent trends, the cost reduction projection appears ambitious. Until a track record for the new centralized Risk Management Division develops, it will be necessary to monitor progress closely and reevaluate projections on an ongoing basis, particularly in light of the impact these substantial expenditures have on the overall budget and the Plan.

The Litigation Management initiative also is key to the reduction in workers' compensation costs. The City is attempting to reduce its backlog of workers' compensation cases by contracting for representation by private law firms. The City has identified 1,100 unresolved workers' compensation cases, and estimates that there could be more than 100 still unidentified. The City's FY94 projection assumes that 800 to 900 of the 1,100 identified unresolved cases will require payment by the City. The unresolved issue is how large the required payments will be. The cases are being evaluated, and over 700 cases have been transferred to outside counsel. Settlements are being negotiated for those cases which present an undue litigation risk to the City. It is assumed that through contracting with private law firms the backlog in cases will be reduced, reducing interest, penalties and other costs resulting from delays. Traditionally, the Law Department has handled these cases, but has not been able to keep up with them in recent years.

CSI Contract -- *Medical cost increases are projected to be well below the expected rate of medical inflation assumed elsewhere in the Plan*

The FY94 budget for CSI is $8.4 million, which includes monthly costs for six months in calendar 1994, and one-time transitional costs of approximately $2.4 million. The total contract amount for calendar year 1994 is $11.9 million ($6 million in FY95). CSI contract costs are projected to increase between 3.5 and 4 percent annually during the FY95-FY99 period. This is based on the assumption that annual medical inflation will be between 7 and 10 percent, and that inflation will be partially offset as a result of medical utilization management and aggressive physical rehabilitation. These offsets will have to result in expenditure reductions of between 3 to 7 percent annually in order to reach the Plan's target levels. There is risk in this assumption. The "worst case" scenario would be a 10 percent annual increase, which is the cap for increases under the CSI contract. Another factor that could change the estimates is a change in the number of active employees under the contract. The City has assumed that the number of active employees would not change. Since the contract will be renegotiated after calendar 1994, maintaining only a 4 percent increase in costs will require that the cost per employee and the number of employees receiving services under the contract in 1994 remain near the level anticipated when the contract was originally negotiated. The Plan, however, anticipates employment of additional City staff, which would seem to drive up the cost of the CSI contract.

There will be additional costs in the FY94 budget for medical care delivered prior to January 1, 1994, which was not covered by the CSI contract. This amount is projected at $1.5 million for workers' compensation cases, and $4.5 million for Regulation 32 and pension cases. These costs could change depending on the City's progress on medical review, case management and other adjustments.

Indemnity Budget--*The City's projections are sensitive to a variety of assumptions*

The indemnity budget represents one of the major costs that the Risk Management Division is charged with reducing. The indemnity budget increased dramatically in FY93 and FY94, a residual effect of the fiscal constraints of the FY89-FY91 period, when the City deferred settlement on many claims to avoid expenditures.

Delays in settlement can cause additional costs due to delay damages and the higher awards that can result if a plaintiff's condition worsens over time. The recent rise in indemnity costs is also due to the Court of Common Pleas' "Day Backward/Day Forward" program to reduce the backlog in case inventory for cases generally, including cases involving claims against the City. FY94 indemnity costs have been partially financed from a special Indemnity Account, which was created with $23.5 million in proceeds of PICA's 1992 bond issue not needed to fund the City's initially anticipated FY92 deficit.

There are risks inherent in the Plan's projection for indemnity costs. A number of assumptions are made in projecting the indemnity budget, such as the number of cases settling, the percentage of cases settling with payment, the average settlement per case and the percentage of costs to be borne by the General Fund. Some of the key assumptions are: special litigation and appeal losses will decline significantly from their FY94 level of $24.7 million to $5.7 million in FY95 and $8.3 million in FY96-FY99 (this is a significant decline from the first draft of the FY95-FY99 Plan); the average settlement for ongoing inventory cases will increase at 3.5 percent annually; and the average settlement for day forward cases will not increase from FY94 to FY96. Only with the passage of time will the validity of such assumptions be known.

The Plan alludes to the use of $7.8 million in proceeds from the PICA Series of 1992 bond issue not needed to fund an anticipated FY93 deficit to add additional funds to the Indemnity Account. PICA Staff has not reviewed the status of the indemnity program since the Authority provided the initial funding, and the City has not yet requested PICA to provide such assistance. If PICA were to agree to add additional funds to the Indemnity Account, the money would be deposited in the Grants Revenue Fund, and would not impact the Plan.

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PRODUCTIVITY BANK

Productivity Bank Loan Authorization Schedule ($ Millions)			
Department/Project	FY93	FY94	FY95
Fleet Management - Alternative Fuels	$ .120		
Fleet Management - Information System		$ 1.944	
Human Services - Child Placement	.051		
Law - Automation	.700		
Police - Photo Automation		1.283	
Public Property - Light Bulbs	.200	.150	
Records - Automation		1.850	$2.0*
Revenue - Integrated Tax System	.750	4.058	
Revenue - Earnings Tax	.200		
Revenue - Automated Audit	.300		
Revenue - Real Estate	.125	1.361	
Streets - Geographic Information System		1.215	
Total Loans	$2.446	$11.861	$2.0

* Council Approval Still Pending

Introduction

PICA, as a portion of its initial 1992 Bond issue, borrowed $20 million for the City's use to establish a Productivity Bank. The funds were to be used to fund productivity initiatives requiring initial capital investment. The Bank's assets were to be replenished from loan repayments by departments receiving the loans (for cost reduction initiatives) and by proceeds from asset sales and other available sources (for "loans" made for revenue enhancement where the particular department received no direct budgetary benefit).

To be eligible for a loan from the Productivity Bank, departments were to be required to be able to demonstrate that projected savings would equal at least twice the amount of the loan or provide sufficient additional City revenues (revenues exceeding FY92-FY96 Plan projections) to pay back the loan plus interest (the rate to be determined on a loan-by-loan basis).

Restoring Productivity Bank Capital -- *The City has yet to finalize procedures to restore borrowed capital to the Productivity Bank*

As a part of the original agreement to create the Productivity Bank the City assured PICA that all of the loans would be repaid either through departmental appropriations resulting from budgetary savings, by utilizing revenue generated by productivity initiatives or by proceeds of City asset sales. Currently several of the authorized loans are budgeted to be repaid through departmental savings in both FY94 and FY95. PICA Staff remains concerned that the process of repayment of loans for revenue generating initiatives has not been finalized, although loan disbursements in most cases are well underway. In order to budget for departmental repayments of loans designed to produce additional revenues, the City would have had to increase the appropriation power of the department based on speculative revenues, and as a policy procedure this would not be practical. Foreseeing this problem, the City indicated that it would review replenishing the Bank with proceeds of City asset sales or ultimately budget loan repayments as a non-departmental cost. This policy has not yet been finalized by the City. PICA Staff encourages the City to finalize the procedures to replenish the Bank through dedication of the proceeds of City asset sales or other means. Current Monthly City Managers Reports indicate that of the $16.307 million principal amount in authorized loans detailed above, $6.794 million relates to loans on which "repayments are contingent on revenue generation exceeding FY92-96 Five Year Plan projections." The remaining loan amounts are categorized as planned repayments from departmental budgets; departments seeking renegotiation of loan agreements and payment deferrals; and payments to be made by Finance Department out of savings on fringe benefit costs. Productivity Bank-financed projects are also hard to assess in light of previously-discussed weaknesses in the City's cost allocation systems.

As a general matter, PICA Staff has expressed reservations about the City's ability to administer a true "loan" program from the beginning of the Productivity Bank process. It now finds itself in the position of once again pointing out that the concept was flawed from its inception and relied upon a non-existent system to handle repayments for revenue generating initiatives. PICA Staff again urges the City to review the process and determine whether it has the capacity to administer the program as first articulated by the Administration and to make necessary changes to make the process credible.

FIRE DEPARTMENT

Primary Areas of PICA Concern
o Overtime
o Zero Salary Growth in FY98 and FY99
o EMS Collections
o Water Fund Payment
o Firefighting Infrastructure

Plan Expenditure Projections FY95 - FY99 (millions)		
	FY95	FY95-FY99
Class 100	$103.3	$531.8
Class 200	3.3	16.7
Class 300	4.4	22.7
Class 800	5.1	26.2
Total	$116.1	$597.4

Introduction

Fire Department Plan-projected total obligations for FY99 total $8 million more than its FY94 Plan-projected obligations. The major component of the Department's projected increase in costs is Class 100 expenditures which are estimated to grow by $2.7 million (2.6 percent) in FY95, $2.6 million (2.5 percent) in FY96, $1.6 million (1.5 percent) in FY97 and then show zero growth for the Plan's two remaining years. The major factor contributing to the increase in early Plan years' Class 100 costs is the anticipated impact of the Act 111 arbitration award. The award instituted new minimum staffing requirements higher than those used to project costs in earlier five-year financial plans. The Administration has indicated that this portion of the award foreclosed it from saving approximately $5 million annually. The arbitration-imposed staffing requirements are now being appealed by the City.

Fire Department cost saving initiatives had little success in FY94, primarily as the result of delays in, and the provisions of, the Act 111 arbitration award. The Department had anticipated that its two primary initiatives (Ladder Company Restaffing and Reorganized Deployment) would decrease personnel costs by $5.8 million annually. Loss of the right to implement these initiatives has resulted in an escalation of overtime costs, although the Department aggravated its overtime problem by delaying a new firefighter class anticipating the arbitrators' award of lower starting salaries. The Department currently projects its FY94 overtime cost to be $3.2 million over budget.

Current projections indicate that the Department's only revenue initiative, Increased EMS Collections, is lagging behind original projections. The projection for FY94 revenues from this initiative was $2.4 million in the FY94-FY98 Plan. The Department currently projects the initiative will generate $1.6 million in FY94 revenues, a $800,000 shortfall. The Department's FY94 projection for total EMS revenues (inclusive of the expected return from the initiative) is currently $7.8 million, or $300,000 less than originally projected. The Department projects $8.1 million in EMS revenues for FY95, growing to $8.5 million in FY99.

Overtime -- *As a result of Act 111 arbitration-mandated minimum staffing requirements, the Department may find it difficult to reduce overtime*

The Act 111 interest arbitration award requires minimum staffing levels as follows:

- One officer and four firefighters for each ladder company;
- one officer and three firefighters for each engine company;
- one officer and five firefighters for heavy rescue companies; and
- one officer and seven firefighters for task force groupings of an engine and ladder company.

The net effect of the award is the need for 144 additional firefighters, with related personnel distribution problems and overtime costs. Testimony given by the Fire Commissioner at the Department's FY95 budget hearing indicated that FY94 costs increased $4.3 million (4 percent) over the Department's original FY94 budget as a direct result of the arbitration award. The Department had anticipated reduced overtime costs resulting from the staffing initiatives sidetracked by the arbitrators.

While PICA Staff feels comfortable with the FY95 Class 100 projection, the projections in the Plan's out-years appear to be somewhat optimistic. The current arbitration award provides for a 3 percent across-the-board raise for all firefighters in mid-FY96, and while PICA Staff realizes that attrition and lower starting salaries should contribute to savings, it nonetheless appears the Fire Department would have to strenuously control overtime over the life of the Plan to stay within current annual projections. Unless the Department is fully successful in its appeal of the arbitration award it appears very optimistic to assume little or no growth in overtime. PICA Staff will continue to monitor the progress of the appeal and overtime costs.

Salary Growth -- *Class 100 obligations are projected at zero growth in FY98 and FY99*

The City has the responsibility to make its own policy decisions. Nonetheless, its assumptions as to the terms of the next arbitration award appear to be optimistic. PICA Staff would caution the City as to the potential negative fiscal impact of overly-optimistic plans for cost containment, and will continue to monitor this cost area carefully.

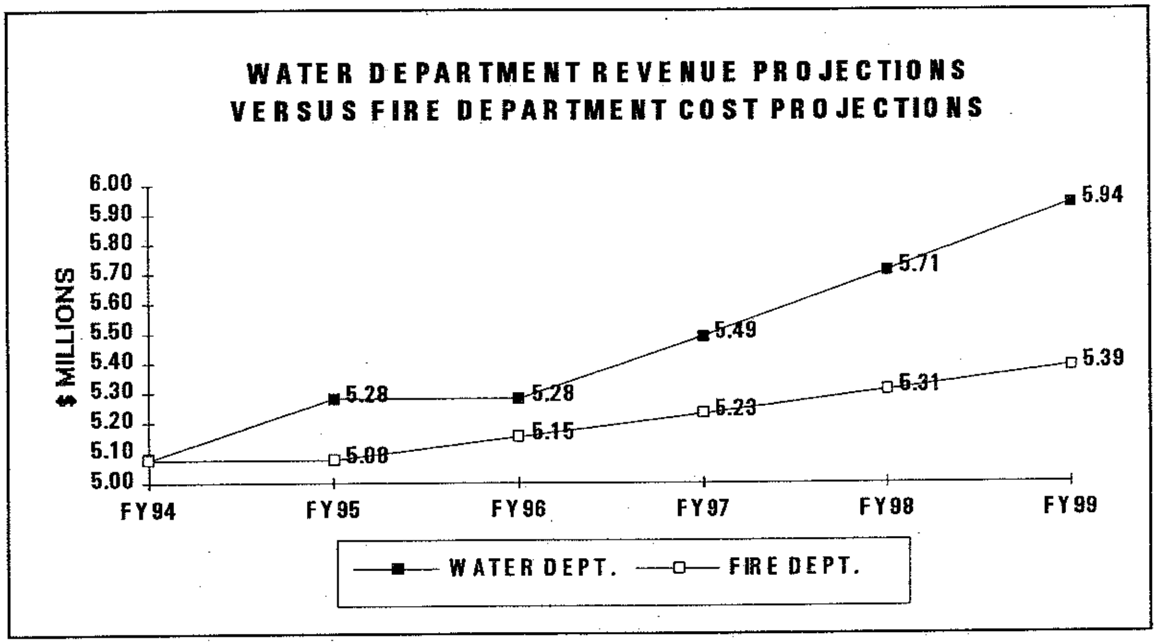
EMS Collections -- ***Reduced demands for service and continuation of lower than expected revenue collections could decrease anticipated EMS revenues***

In order to improve response time, the Department has indicated that it is considering reducing the work load of its medical response teams by contracting out a portion of EMS services. Depending upon the contractual terms, this could decrease EMS revenue collections and, as per Department indications, the prospect for letting such contracts has not been built into the Plan. Partial privatization of EMS is not anticipated to affect FY95, but it may affect the out-years of the Plan. Since FY94 EMS revenue projections are lower than originally anticipated (by $300,000), and given the possibility of partial privatization of services, the Plan's EMS revenue estimates may be optimistic; and it is not clear whether the Department would obtain any significant Class 100 savings. Contracting out EMS services probably would result in higher Class 200 expenditures.

Water Fund Payment -- ***The Department's projected growth rate for payments to the Water Fund for fire hydrant water usage is not consistent with that of the Water Department***

In previous reports, PICA Staff has encouraged the City to allocate operating costs back to the responsible departments properly, and to do so on a consistent basis. One area where the City attempts to make such an allocation is water costs, and one of the departments that is charged for the use of water is the Fire Department. Historically, the Fire Department has paid for the use of water based on the number of fire hydrants in use during the year. A part of this calculation takes into account rate increases consistent with those applicable to residential consumers. Recently, the Water Department won the right to increase water bills annually based on the Consumer Price Index (CPI).

In the Official Statement for its 1993 Series Water and Wastewater Revenue Bonds, the Water Department projected an annual 4 percent increase (with the exception of FY96 when there is no increase) in revenues utilizing the rate increase formula. The City, for the benefit of the Fire Department, utilizes a 1.5 percent annual rate for water cost increase projections. The Plan assumes 3.5 percent as its general inflation factor after FY94. The chart below illustrates the differences between the Fire Department and Water Department projections using FY94 as the base year:



While the monetary difference disclosed in the above graph is not a material amount in the context of this Department's overall annual expenditure projections or the Plan, similar inconsistencies in other departments could combine to total a meaningful sum.

The inconsistency depicted above highlights a methodological weakness in the Plan preparation process. Achieving a 1.5 percent annual growth assumption for CPI over five consecutive years is highly unlikely, and utilizing different rates for the same item (between funds) has no rational basis. Utilization of inconsistent and unrealistic assumptions within the Plan diminishes the benefits that cost allocation (and the Plan itself) provides as a management tool. PICA Staff encourages the City to use appropriate and consistent cost allocation methodology.

Firefighting Infrastructure -- ***The disposition of the City's fire facilities remains primarily unchanged from a different era***

In previous reports, PICA Staff has suggested that a comprehensive citywide facilities assessment study (similar to the Police and Prisons facility assessment studies) would provide the City with a structural assessment that would set guidelines for repairs and further provide the ability to perform the appropriate cost-benefit analysis that ultimately should determine continued use or replacement/disposition of facilities. As well, such an assessment would lay the foundation for a broader analysis of the efficiency of the current facilities in times of changing community needs. The Fire Department has stated that it has developed a comprehensive view of its priorities without the benefit of outside assistance.

The Plan states, "The City's firefighting infrastructure, however, remains constructed for a different era. Fire stations are still sited for population patterns that have shifted substantially since the stations were built, while the Department's Engine and Ladder Company system was structured for a significantly larger force." The still-frustrated attempt by the Rendell Administration to impose lower staffing requirements on the Department, if successful, would have permitted the City to recognize some savings. Ultimately, as the Commissioner has noted, the City has to come to terms with its operational systems.

While no timetables have been set, the Department has pledged to explore both new technology and organizational changes to improve future efficiency. PICA Staff, acknowledging the progress the Department has shown in addressing the effects of long-neglected facility improvements and maintenance, is still very concerned that no geographical changes are being currently proposed in either the Plan or the City's capital budget for FY95. We are aware that any proposal relative to closing or relocating fire stations prompts immediate unrest among community groups and others seeking to retain the *status quo*. Nonetheless, this is a major problem that must be addressed promptly by the current Administration if the City's firefighting infrastructure is to meet the demands placed upon it in the decades ahead.

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DEPARTMENT OF HUMAN SERVICES

Primary Areas of PICA Concern

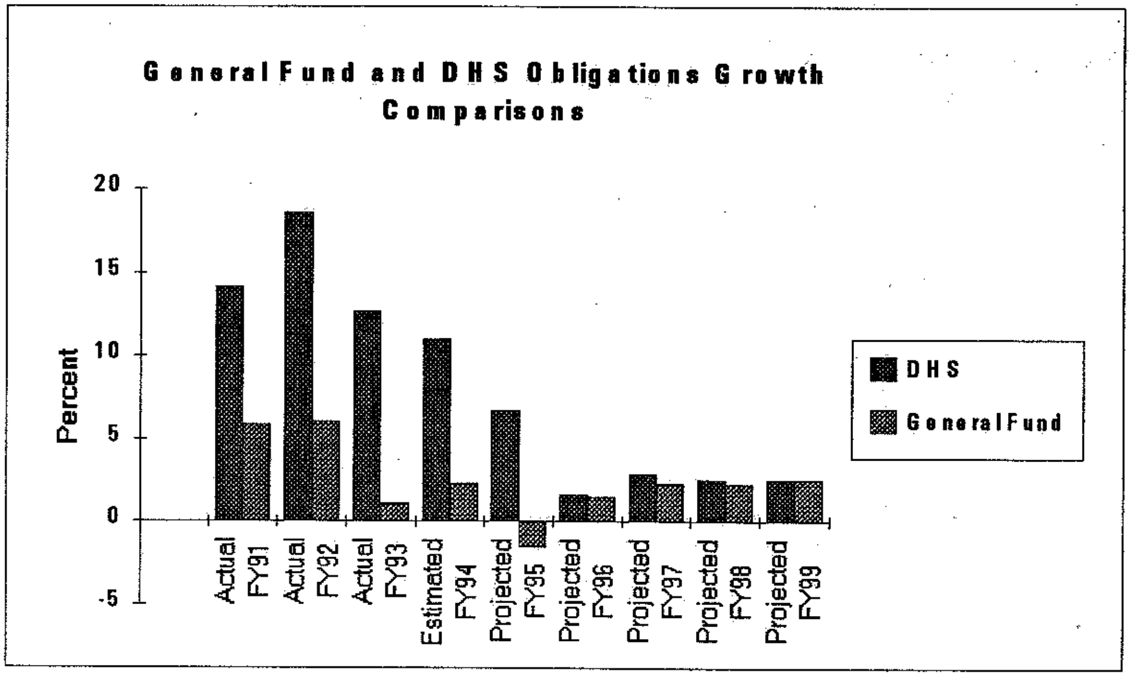
- o Revenue Projection Methodology
- o DHS Staffing Projections
- o Anticipated Cost Diversion
- o Dependent Children Purchased Service Rates
- o Reduction in Restrictive Placements
- o Moderate Growth in Days of Service
- o Title IV-A Funding Risks
- o Calculation of Reimburseable Costs
- o State Budget Funding Shortfall

Plan Expenditure Projections FY95-FY99 (millions)

	FY95	FY95-FY99
Class 100	$ 44.5	$ 232.6
Class 200	239.2	1,254.8
Class 300	1.6	8.2
Class 400	2.1	11.2
Class 500	0.1	0.3
Total	$287.5	$1,507.1

Introduction

Department of Human Services (DHS) General Fund obligations have grown much faster than General Fund obligations overall since FY90, as shown in the graph below. The Plan projects that DHS General Fund obligations will grow at an annual average rate of 3.4 percent from FY94 to FY99, a rate much closer to the projected overall General Fund obligations growth rate than has been achieved in recent years. This would constitute the most significant cost containment action of any City department, if it can be accomplished.



Accomplishing this turnaround would require positive outcomes on a number of fronts. The most significant risks to the DHS portion of the Plan appear to be on the expenditure side, where aggressive assumptions have been made by the City about growth rates in the number of cases overall, and particularly as to growth rates in the number of high cost placement cases. The most aggressive assumption relative to expenditures concerns the cost of service. The cost of a day of service is projected to remain constant beyond FY95, without even an inflation increase, for nearly all types of purchased services. Since a significant portion of such costs involve medical services, this assumption is aggressive. There are also risks on the revenue side, where projected growth rates, although modest, are calculated from a FY95 base that may be substantially above the level of revenue DHS may actually receive, given the State Department of Public Welfare-certified FY95 budget for DHS. Another major concern for FY95 and beyond is the need for State approval of contemplated diversion of funding for certain additional categories of medical service costs to the Medicaid program.

The combined impact of the preceding expenditure and revenue risks in the DHS projections could have a significant detrimental effect on the overall Plan. These budget risks are more fully discussed below, along with several methodological issues. PICA Staff cautions that DHS unreimbursed costs were a significant factor in the accumulation of past General Fund deficits and that future cost-to-revenue disparities must be closely controlled and directly addressed on a timely basis.

The actions DHS proposes to take represent a significant change in focus to emphasize prevention, and a move toward State goals which if successfully implemented could result in both operational and financial improvements.

DHS Revenue Projection Methodology -- ***Improvements have been made during the Plan review process in projecting Title IV-E and Act 148 revenue***

DHS provided its methodology for estimating Title IV-E revenue in FY94 and FY95 to PICA Staff. The calculations are based on the estimated placement costs for dependent and delinquent children, reduced by non-eligible costs (such as costs for placement in for-profit institutions and emergency shelter costs). The resultant eligible costs are multiplied by factors for the client eligibility rate (81.4 percent) and the Federal financial participation rate. In addition, an administration and training component is estimated in the calculation. The projection methodology appears reasonable to PICA Staff, insofar as it goes. An additional factor, not taken into account in estimating FY94 revenue or obligations, is the FY94 diversion of $7.3 million in foster family medical care costs to Medicaid. This diversion will reduce the Department's placement costs in FY94, and the amount of IV-E revenue for which it would be eligible will be reduced by approximately $2.9 million as a result. DHS expenditures would decline by $4.4 million.

In the original version of the Plan, the same method used for estimating IV-E Revenue in FY94 and FY95 was not applied in making estimates of IV-E revenue for FY96 through FY99. In the revision of the Plan incorporating supplemental information and technical modifications, the City adopted PICA Staff's suggestion to utilize the same methodology for projecting IV-E revenues in all years of the Plan. The result was a reduction in projected IV-E revenue by $6.5 million.

Act 148 revenue projections, which are projected to increase at the rate of overall DHS obligations including fringe benefits, less Title IV-E reimbursements, were also changed to reflect the impact of changes made to Plan projections of Title IV-E revenues and personnel costs, for a net reduction in Act 148 revenues of $0.6 million.

DHS Staffing Projections -- *The Plan depends on a continuation of low growth in caseload*

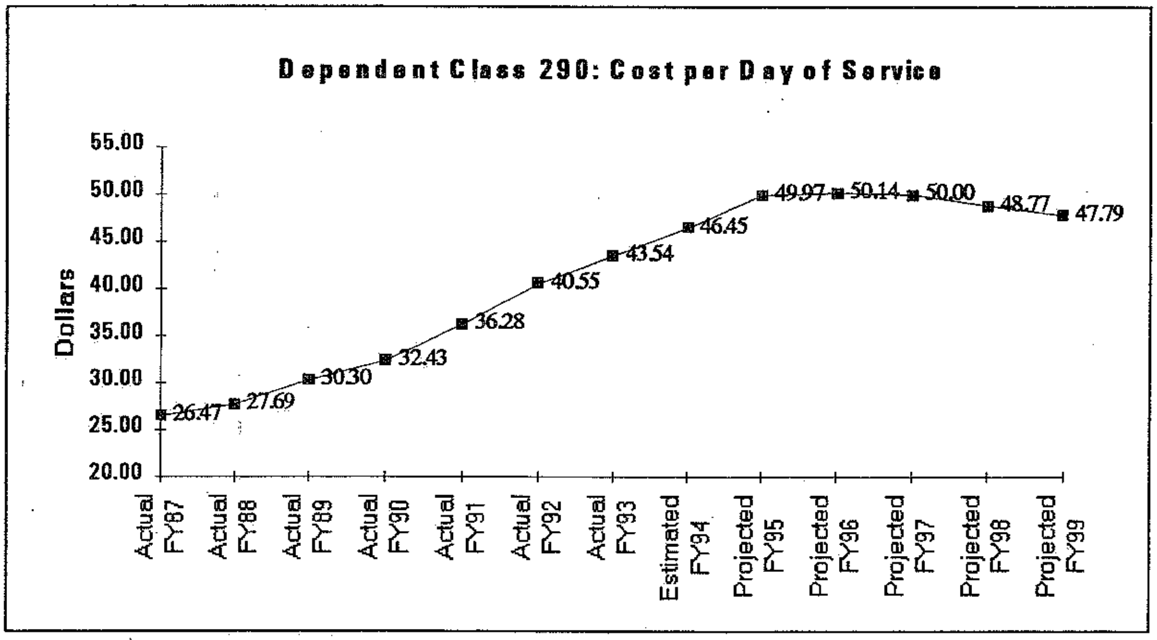
The original version of the FY95-FY99 Plan projected a level personnel complement for the entire five years of the Plan. PICA Staff, in the course of its review of the Plan, expressed concerns that this was inconsistent with a projection of 5 percent annual increases in the number of dependent children receiving purchased services, given State mandates to maintain a certain ratio between caseworkers and the number of families receiving services. DHS responded that this reflected an assumption that while the total caseload would remain constant, a larger portion of that caseload would receive purchased (as opposed to direct) services. Through supplemental information and technical modifications to the Plan, the City anticipates increased staffing and personnel costs (both salary and benefits). DHS staffing is projected to increase by 11 positions in FY96, and by 10 positions in FY97, FY98 and FY99. The Plan thus assumes a fairly low rate of growth in the total caseload of children served by DHS, which will depend on the continuation of recent trends.

Diversion of DHS Costs to Medicaid -- *Plan expenditures are reduced by $35 million on the assumption that Medicaid will cover the cost of some types of services which the State has not yet acknowledged are Medicaid-compensable*

The Plan assumes the cost of some contracted medical services to dependent children will be covered by Medicaid under the Early and Periodic Screening, Diagnosis and Treatment program. Some of the types of medical services projected to be diverted to Medicaid have not yet been approved for diversion by the State. Diversions are projected beginning in FY96 for psycho-social rehabilitative services that are not currently Medicaid-compensable. These anticipated diversions result in $35 million in reduced expenditures over the life of the Plan, beginning in FY96. Day treatment costs of $5 million are projected for diversion in FY96-99, although DHS is currently awaiting a statement of "concerns and issues" from DPW relating to it. The potential risk to the Plan of not receiving State approval to divert these costs is $40 million in increased expenditures. If these increased expenditures would continue to be reimbursed at a 75 percent rate, the net adverse impact would be $10 million in the FY96-FY99 period.

Dependent Children Purchased Service Rates--*The projected zero rate increases for service contracts for dependent children is extremely aggressive, and poses a significant risk to the Plan*

Despite steady increases in recent years in the cost per day of contracted services for dependent children, the Plan assumes that increases will cease for all categories except foster care for all of the years of the FY95-FY99 Plan. There is a significant foster care rate increase projected to take effect in FY95, but none after that, and thus even foster care rates are projected to grow at rates below inflation over the five years of the Plan. These projections appear aggressive since they represent a distinct departure from historical patterns. For most categories of service there has been a smooth trend of annual cost increases each year, and Class 290 per diem costs in the FY87-FY93 period grew by 60.8 percent (versus a Plan-projected FY93-FY99 growth of 9.8 percent). The Plan anticipates arresting this growth at FY94 levels. The chart below presents past and projected cost per day of service for DHS Children and Youth Division purchased services.



Aside from the discontinuity from trends projected by the Plan, the more basic reason why these projections appear aggressive is that the zero growth projection is based on per diems before diversion, which represent full costs, both medical and non-medical. A significant portion of these full costs are for medical services, a cost component highly unlikely to grow at rates significantly below the Plan's assumed 3.5 percent inflation rate. Elsewhere in the Plan medical costs have been assumed to range up to a 12 percent annual growth, compared to a general inflation rate of 3.5 percent. Although the City may obtain relief from most of the medical components of these costs, the projection subtracts diversion savings from the projection of total costs.

PICA Staff calculated the impact on Plan expenditures under the alternative assumption that per diem rates generally will grow at 3 percent annually, which is still a conservative assumption, given that general inflation is projected in the Plan at 3.5 percent, and medical inflation is projected at 12 percent for the purpose of estimating City employee health benefits. Under this scenario, expenditures would be $71 million higher than in the current Plan. Since DHS expenditures on average are reimbursed at a 75 percent rate, the net adverse effect on the Plan would approximate $18 million.

The Department recently engaged the Child Welfare League of America (CWLA) to review its rate structure, but subsequently terminated the study after determining that the parameters proposed by CWLA for the study were not acceptable. The City, after several PICA Staff requests, refused to provide the preliminary material developed by CWLA to the Authority. As an alternative to the CWLA effort, DHS is currently conducting an internal study of its rate structure, which is expected to be complete by the end of calendar year 1994. The results of the internal study are expected to be taken into account in the FY96 budget process. Absent such a study to provide support for the current budget and Plan, the current rate projections can only be characterized as highly aggressive and as posing significant risks to the Plan. The involvement of CWLA in the work of DHS has been a source of comfort to those who have misgivings about DHS' capacity to manage its own affairs. The termination of its work in this area, and the City's refusal to share the CWLA work product upon which the termination decision was based, does little to build confidence in the Department.

Reductions in Restrictive Placements -- ***The Plan projects that the percentage of DHS caseload being served in the most expensive, most restrictive placements will decline, a goal which poses some risks to the Plan if not fully achieved***

Another key assumption in the Plan is that DHS will be able to redirect large portions of its overall caseload into less costly types of service. Significant growth is projected in comprehensive family preservation, day care and adoptions and moderate growth or zero growth in other categories of service. If this assumption does not hold true, and growth in caseload is equal among categories, expenditures could be $20 million higher than in the Plan, with a net adverse Plan impact of $5 million after reimbursement. If a 3 percent increase in per diem rates is also assumed, expenditures would increase by $92 million, with a net adverse impact of $23 million after reimbursement. In order to meet its goal, DHS must radically alter its service delivery systems, and it has had only modest success in similar prior efforts.

Moderate Growth in Days of Service -- *Growth in the number of days of service provided has moderated in recent years, and the Plan assumes that this trend will continue*

Overall growth in the number of days of service provided through DHS is projected to decline over the Plan, from levels as high as 12 percent in recent years (7.5 percent currently) to 5 percent in the last four years of the Plan. If days of service were to continue to grow at the rate of 7.5 percent annually for all categories (the level of growth currently projected for FY94) expenditures would increase by $80 million over Plan levels, for a net adverse impact of approximately $20 million. If per diem growth of 3 percent is also assumed, expenditures would increase by $157 million, with a net adverse impact of $38 million after reimbursement.

Title IV-A Emergency Assistance Funding -- *The proposed FY95 Commonwealth budget assumes a new source of funding which is uncertain in both the short- and long-term*

The proposed State budget for FY95 assumes that funding will be obtained from the emergency assistance portion of the AFDC program, Title IV-A, to support county child welfare programs statewide, beginning in January of 1995. There is a question whether the State can develop a plan, receive Federal approval, and develop eligibility and monitoring processes in time to assure implementation by January. Eligibility determinations will have to be carried out for a large number of cases, not simply the relatively small number of cases in placement (as is the case with the IV-E program). In addition, the IV-A emergency assistance program has been cited as being among the programs that may be cut to fund a possible Federal welfare reform package. As a result, there are both short-term implementation risks and long-term funding risks associated with this projected revenue source.

Calculation of Reimbursable Costs -- *DPW recently has questioned the validity of past DHS billings for personnel costs, which may affect future Act 148 revenues*

A recent DPW review of DHS personnel practices found that Philadelphia social workers work a 37.5 hour work week, rather than the 40 hour week that DPW had been assuming since FY84 in calculating the hourly rates of DHS social workers. The effective increase in the hourly rate used by DPW will reduce the amount of DHS expenditures considered reimbursable by the State under Act 148, since Philadelphia DHS salary rates are already above the level the State considers reimbursable. The State has indicated that, in its opinion, retroactive adjustments should be made to Act 148 reimbursements that have been received by the City since FY84. Given that the State was not fully funding its Act 148 obligations during portions of this period, however, it does not seem there should be a direct relationship between a reduction in the City's reimbursable costs under Act 148 and an equivalent reduction in State Act

148 reimbursement, for at least those years in which Act 148 revenues received by the City were not based on actual reimbursable costs under Act 148. This matter could result in a reduction in State Act 148 revenue in the future, both as a result of retroactive adjustments, and reductions in future reimbursement levels, and PICA Staff will monitor the issue as it develops.

State Certified FY95 Budget -- ***The FY95 Department of Public Welfare-certified budget for DHS provides State and Federal revenues that are below Plan levels, and revisions to the Plan will be needed as a result***

There are a number of discrepancies between the Plan and the FY95 DHS budget as certified by DPW. The DPW certified level of IV-E revenue is $89 million, compared to Plan level of $91.4 million. Further, the City expects to receive less than the DPW-certified amount by $0.9 million by not having funds available for investment. The City projects that it can make up some of the difference in IV-E revenue by transferring contracts from for-profit agencies, whose services are not eligible for IV-E reimbursement, to non-profit agencies.

State certified Act 148 revenue, inclusive of State appropriations and Federal Title IV-A and Title IV-B funds, is $127.6 million, or $8.9 million less than the City has budgeted for FY95. The City expects to make a portion of this gap up through additional IV-E revenue received for placements in State Youth Development Centers. This could reduce the apparent shortfall to $7.1 million.

Such a shortfall in both Act 148 and Title IV-E revenue in FY95 would require adjustments to the Plan for the FY95 to FY99 period, since FY96-FY99 revenues in the Plan were projected on the basis of the City's assessment of anticipated FY95 receipts. Information received from the City indicates that the DPW-proposed need-based budget for the Commonwealth was larger than the amount proposed by the Governor. The City has represented that it is prepared to pursue all appropriate avenues, including litigation, to ensure that appropriate levels of Act 148 reimbursements are obtained. PICA Staff is of the opinion that it is likely that the proposed State budget does not provide appropriate Act 148 funding for DHS. As a result, projections as to Act 148 funding beyond FY95 have a speculative element, which has significant budgetary impact throughout the Plan's term.

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POLICE DEPARTMENT

Primary Areas of PICA Concern

- o Overtime Costs
- o Special Events Reimbursements
- o Decline in Moving Violation Citations Issued
- o Non-Emergency Transportation
- o Abandoned Vehicles Initiative
- o Helicopter Unit
- o Federal Crime Bill

Plan Expenditure Projections FY95 - FY99 (millions)

	FY95	FY95-FY99
Class 100	$290.5	$1,496.8
Class 200	4.8	23.4
Class 300/400	6.9	36.2
Other	.4	1.0
Total	$302.6	$1,557.4

Introduction

The Plan states that "the mission of the Police Department is to enhance the quality of life for City residents by enforcing law, reducing the fear and incidence of crime, and ensuring public order and safety." To ensure this mission is accomplished, the Department has established the following goals:

- o Public Safety - To provide a secure environment that will foster residential, commercial and cultural advancement within the City of Philadelphia.

- o Efficient and Effective Service - To provide quality services through the cost efficient and effective utilization of department resources.

- o Leadership in the Community - To enhance the Police leadership role in the community by providing high quality police services emphasizing fair treatment of citizens.

- o Partnership - To achieve effective citizen, police personnel, public and private agency involvement in the Department's strategies in order to improve the quality of life and enhance public safety.

- o Professional Personnel - To provide a highly motivated and trained work force which is professional, ethical and representative of the community it serves.

The Police Commissioner has stated that despite budget reductions for the Department, focusing on the above goals and on the initiatives set forth by the Administration will allow the Department to continue to meet its commitment to preserve public order.

Projected FY99 Police Department obligations total $17.2 million more than the projected FY94 obligations in the Plan. The major component of the Department's projected increase in costs is Class 100 expenditures which are shown to grow by $4.3 million (1.5 percent) in FY95, $7.3 million (2.5 percent) in FY96, $5.1 million (1.7 percent) in FY97, and then project zero growth for the remaining two years of the Plan. The major reason for the increases in FY95 and FY96 are the across-the-board salary increases (2 percent and 3 percent) which take effect on January 1, 1995 and 1996, respectively.

Overtime Costs -- *The Police Department continues to have problems controlling overtime*

As in the past, the Police Department has had difficulty controlling overtime costs in FY94. The Monthly Managers Report (for the month ending February 28, 1994) projects FY94 overtime costs to be $1.8 million over the adopted budget. The Police Department attributes these costs to special events such as Operation Rescue, Welcome America, the Phillies championship and an unusual number of winter weather emergencies. Reduced force size coupled with events that require substantial police presence contribute to the need for overtime. The Department's plans to control future overtime costs contemplate factors such as lower starting salaries, attrition of higher paid officers, additional street duty officers available as a result of civilianization and charging outside agencies for Police personnel overtime costs. Because of staffing changes, lower starting salaries and minimal salary growth PICA Staff believes the Department's overtime estimates are reasonable. PICA Staff cautions, however, that success in the Department's charge back initiative for special events is important as well.

Special Events Reimbursements -- *Charging groups for Police Department overtime costs during special events has yet to show significant results*

The Police Department initiated a new Special Events policy in FY94. The policy contemplated charging groups for overtime costs resulting from scheduled special events. Upon further review, both the Mayor and the President of City Council concluded that full reimbursement from not-for-profit groups was not practical. To date the Police Department has not collected any significant amount to offset overtime costs from either for-profit or not-for-profit groups. Several special events in FY94 incurred overtime costs in excess of $1 million, none of which has been reimbursed. PICA Staff encourages the Police Department to seek appropriate reimbursement from groups involved in special events in accordance with the guidelines established by the Mayor and President of City Council.

Decline in Moving Violation Citations Issued -- *Moving violation citations issued by the Police Department have decreased precipitously in the past two years*

In Philadelphia's FY92-FY96 Plan, revenue enhancements from increasing the collection rate of moving vehicle violations were projected. These projections did not come to fruition, in part because of a drastic drop in the number of moving violation citations issued. The Police Department has acknowledged a concern relative to this issue and indicates it believes that devotion of resources to other activities was the primary cause of the decline. Philadelphia Traffic Court records indicate that moving violation citations decreased 18 percent from calendar 1991 to calendar 1992 and 25 percent from calendar 1992 to calendar 1993 (38 percent from calendar 1991 to calendar 1993, a difference of in excess of 100,000 tickets). PICA Staff will continue to monitor this situation.

Non-Emergency Transportation -- *The Police Department hopes to end the practice of assigning police officers to transport non-emergency hospital and medical cases*

During FY94, the Police Department instituted a pilot project in the South Philadelphia Police Division aimed at ending the practice of assigning police officers to transport non-emergency hospital and medical cases. The Administration has convened a task force to study the City's EMS system, including the Police Department's role. The City has not yet established a time-table for any such change, nor has it quantified any savings for any of the years in the Plan. PICA Staff believes the goal to be appropriate, but is concerned that this initiative may ultimately result in either decreased EMS revenue collections or increased EMS costs and only a marginal reduction in Police Department expenditures. Accordingly, the results of the study will be closely reviewed when available.

Abandoned Vehicle Initiative -- *The Abandoned Vehicle Initiative is no longer being pursued by the Police Department*

The Police Department had anticipated replacing twenty-three uniformed officers assigned to handle abandoned vehicles with Philadelphia Parking Authority (PPA) personnel. The FY94 savings from this initiative were projected to be $840,420. In a recent meeting with PICA Staff, Police Department personnel indicated that due to both PPA and Fraternal Order of Police resistance, the Department is no longer pursuing this initiative. The Department has indicated that the anticipated savings were built into the Plan for FY95 and the following years, and that equivalent savings will be achieved through other, but not yet specified, initiatives.

Helicopter Unit -- *The Department plans to establish a helicopter unit in FY95*

The Police Department has indicated that it plans to establish its first helicopter unit in FY95. The Department anticipated that this unit's start up costs would be initially funded by the Commonwealth; however, the State's FY95 capital budget does not include funding for either helicopters or personnel. The Department anticipates that this unit would assist in improving response time and in decreasing indemnities costs resulting from high speed automobile pursuits. The unit is to include 18 pilots, none of whom have been provided for in City or State budgets. The Department projects annual operating costs of between $1.1 to $1.5 million. PICA Staff acknowledges the potential benefits which could result from this new unit, but is concerned that neither capital nor operating costs have been adequately planned or provided for. PICA Staff will monitor this area very closely.

Federal Crime Bill -- *A portion of President Clinton's proposed crime bill partially subsidizes salaries of additional police officers for municipalities for up to five years*

President Clinton, in the proposed Violent Crime Control and Enforcement Act, has proposed a Federal program which would partially subsidize the cost of additional police personnel for municipalities for up to five years. The Police Department, PICA Staff and some public officials from other jurisdictions have expressed the concern that this program could provide increased police presence in the near term at 25 percent of the normal cost but subsequently require local government to absorb the total personnel costs. Thus, a uniformed officer level could be established which the Department would ultimately be required to maintain without supportive outside funding. The details of this legislation, if an when approved by Congress and signed by the President, merit scrutiny.

PRISONS DEPARTMENT

Primary areas of PICA Concern

- o Construction Delays
- o Holmesburg Demolition
- o Prison Health Contract/Population Projections
- o Food Service Contract
- o Preventive and Normal Maintenance

Plan Expenditure Projections
FY95 - FY99
(millions)

	FY95	FY95-FY99
Class 100	$63.2	$326.2
Class 200	$13.6	70.0
Class 300/400	5.1	26.1
Class 500	.6	3.3
Total	$82.5	$425.6

Introduction

The mission of the Philadelphia Prisons System (PPS) is the maintenance of a correctional program that adequately confines individuals accused or convicted of illegal acts. Simultaneously, the Prisons system provides human services, supervision, training, and rehabilitation in the hope that incarcerated individuals will eventually be functional and productive members of society subsequent to their release.

The Philadelphia Prisons System primarily provides correctional services at five institutions: Holmesburg Prison, House of Correction, Philadelphia Industrial Correctional Center, Alternative and Special Detention and the Detention Center. Currently under construction is the Curran-Fromhold Detention Facility, a new 2,000 bed institution which is now anticipated to open in September 1995 (approximately one year behind schedule). Curran-Fromhold will replace the obsolete Holmesburg Prison, which is to be closed. The Prisons System is also planning the construction of a new facility which is hoped to open in mid-FY96, and intended to replace the House of Correction and its modular addition.

The Plan projects Prisons System expenditures to be $82.5 million in FY95, a 7.1 percent increase over the Plan's FY94 estimates. The Prisons System's expenditures are projected to grow 2 percent in FY96 and FY97 and .04 percent annually thereafter through FY99. The Plan projects cumulative obligations for the Prisons System totaling $425.6 million. Two major changes in the Prisons System's FY95 costs result from the privatization of food services (which increased Class 200 costs by $6.6 million and decreased Class 300 costs by $5.9 million) and the now delayed scheduled opening of Curran-Fromhold in mid-FY95. The two factors produce a net increase in Class 100 spending of $5.5 million, but it is important to note that the end result is also the creation of 1,000 additional beds in Philadelphia's presently over-crowded correctional facilities.

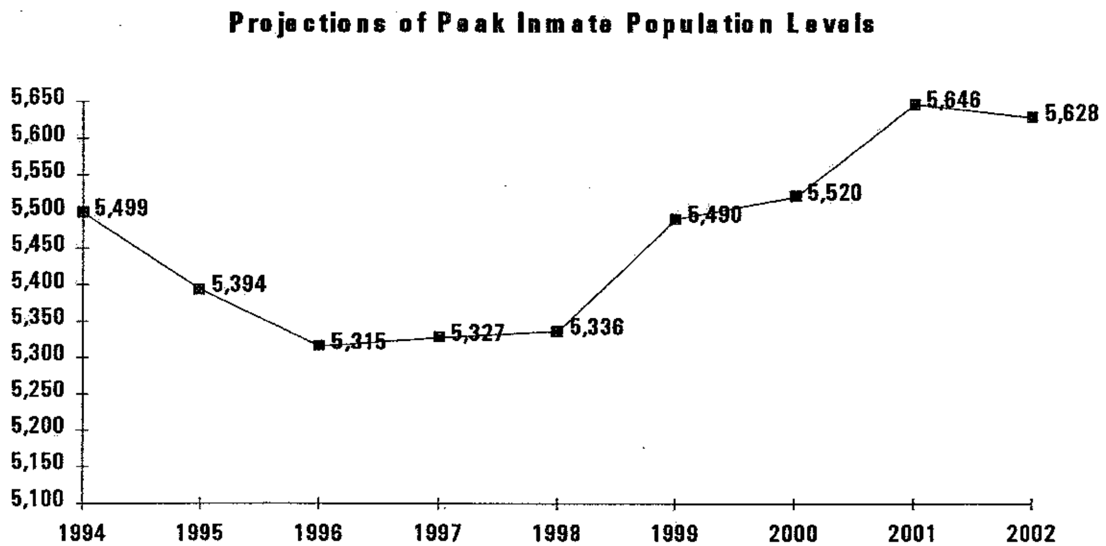
In previous reports, PICA Staff encouraged facility assessments for City-owned properties in order to better set priorities for capital spending and to aid in the creation of a preventive maintenance program. PPS recently performed such an analysis of its facilities while developing a ten-year capital improvement plan. Some of its findings are summarized below.

Philadelphia Prison System's Ten-Year Capital Improvement Plan

Pursuant to a court order and in an effort to assess the current physical condition of the system, the City commissioned a physical and functional audit of Prison System properties. Utilizing the results of this audit, the City developed a Prisons System ten-year capital improvement plan. The goal of this plan is to ensure that the City has the capability to provide (1) sufficient bed space for all PPS inmates, (2) appropriate bed space based on inmate classification level and (3) a prison system whose facilities meet court-imposed standards.

In order for the capital plan to project the Prisons System's future capacity requirements accurately, it was necessary to get an understanding of PPS' current inmate capacity levels. This was done by taking an inventory of all confinement units throughout the Prisons System. A total of 5,616 beds were identified; however it was determined that actual capacity could be as low as 3,549 beds due to inoperable cells (resulting from poor maintenance) and prisoner housing standards established under the *Harris* Consent Decree.

To establish future capacity requirements, the City retained the National Council on Crime and Delinquency (NCCD) to perform population projections. The projections, based on data gathered in July 1993, are noted in the chart below.



Source: NCCD July 29, 1993 Projections.

The chart indicates that inmate population levels are projected to be relatively stable through the year 2001. For at least some budgeting purposes, the City has projected the population level to be 5,600 in FY95 growing to 6,000 in FY99. Delays in completion of Curran-Fromhold will influence these projections.

In order to meet the projected population demands depicted in the above chart, the PPS ten-year capital improvement plan anticipates four major courses of action:

Construction of Curran-Fromhold (CFCF) and closure of Holmesburg Prison

PICA, in its 1993 bond issue, borrowed $53.6 million to fund Phase II of the Curran-Fromhold project. Once completed, this facility will have the capacity to house 2,000 inmates, replacing the much less efficient Holmesburg Prison which then will be closed. The completion date for this project was tentatively set for June 1995 with the first 1000 inmates relocating as early as February 1995. It is likely that there will be substantial slippage in this schedule. The net effect to the Prison System will be an additional 1,000 beds.

Construction of a new 1,250-bed low security facility to replace the House of Correction, Modular 1 and an existing warehouse

The Capital Plan also anticipates construction of a 1,250 bed low security facility to replace the House of Correction, its Modular 1 component and an existing warehouse. The new facility is scheduled to open on December 31, 1996, and the estimated cost is projected to be $45 million. The Philadelphia City Planning Commission's (PCPC) recommended FY1995-FY2000 Capital Program contemplates expenditures of $5 million in FY95, $25 million in FY96 and $15 million in FY97 for this purpose.

Improvements to existing facilities

The PPS capital plan also anticipates correction of deficiencies at the Detention Center and the Philadelphia Industrial Correctional Facility (PICC) discussed in the facilities assessment report. These improvements, once completed, will increase the rated capacity at both facilities (Detention Center - 219 and PICC - 226). The total capital cost for these improvements is projected at $14.4 million. The PCPC-recommended FY1995-FY2000 Capital Program contemplates a combined $8 million for work.

Improvements to the Prisons System's Maintenance Division

Based on results included in its facility assessment report, the PPS capital plan identified the following as Maintenance Division problem areas:

Weak leadership and supervision. PPS acknowledges that maintenance management has exerted little supervision and direction to focus the maintenance work force properly.

Staff Inefficiency. The Division's 130 maintenance workers' primary focus appears to be the protection of overtime benefits, avoidance of supervisory duties and refusal to utilize inmate workers to complete projects.

Absence of Preventive Maintenance Program. Facilities are routinely allowed to deteriorate to the point of crisis before the Division takes notice and responds.

Inefficient processing of work projects and orders. Work orders are not prioritized according to a system. They are under the subjective judgment of the Director of Maintenance. Priorities appear to change according to which facility or staff person exerts the most pressure on the Director.

The Building Services Division of the Department of Public Property has indicated it both will perform additional audits on the PPS Maintenance Division and offer managerial assistance. Privatization of maintenance is another option PPS is reviewing. Under any circumstances, PPS states "a comprehensive preventive maintenance program is to be instituted."

PICA Staff, while pleased with the overall vision and initiative shown in the PPS capital plan, has several areas of concern.

Construction Delays -- *Any further delays in the opening of Curran-Fromhold or the new House of Correction would adversely effect the fiscal situation of the Prison System*

The Plan states that the opening of the Curran-Fromhold facility "will provide a more state-of-the-art facility, easier to operate and manage, and will also increase system capacity to accommodate increasing numbers of inmates." The Plan projects this facility will save the City $750,000 in operational costs annually through more efficient operations. The Plan also acknowledges that any delays in the opening of Curran-Fromhold will have a negative impact on the PPS budget. PICA Staff, recognizing that the opening date had already been extended from September 1994 to February 1995, and that the project is the subject of on-going contractual disputes, recently expressed strong reservations as to its timely opening. Material received by PICA from the City on April 28, 1994 indicate that completion is now anticipated in September 1995, and PICA Staff anticipates the necessity for related adjustments in the Department's budget.

Also, based on the current status of the new House of Correction project, it would appear the Department is unduly optimistic in projecting a December 31, 1996 target date. Currently this project is in the early stages of site location with no FY94 capital funding. The City has budgeted $45 million for this project spread over the next three fiscal years with the bulk being budgeted in FY96. Based on this schedule, PICA Staff surmises that design probably will be completed in FY95 with construction continuing through FY96 and ending later in FY97 than a December 31, 1996 occupancy date would anticipate. While this delay will not affect FY95 PPS operations, PICA Staff anticipates adjustments to the Department's FY96 and FY97 budgets.

Holmesburg Demolition -- *Indecisiveness on the demolition of this facility could jeopardize State Act 71 funding*

PICA Staff has a concern relative to apparent indecisiveness as to the disposition of Holmesburg Prison. In meetings held in May 1993 PICA Staff was advised that this facility had to be demolished or Commonwealth Act 71 funding ($7.8 million) would be forfeited. Recent meetings with Prison Department personnel indicated that while the facility will be decommissioned, no decision about demolition has been made.

Prison Health Contract -- *Accurate population projections are necessary to project future health care costs*

Although budgetary responsibility for prison health care lies with the Public Health Department, PICA Staff believes it appropriate to express a particular concern in this section.

In an attempt to offer more efficient and less costly health care to PPS inmates, the City privatized the services. The cost in FY94 is now estimated at $13.8 million, $3.6 million over the original ($10.2 million) budgeted amount. Both the Health Department and Prison System have a responsibility to project population as accurately as possible. Currently, the Health Department has built its Plan for funding privatized prison health care cost projections on a 5,000 prisoner, no growth, base. Based on the population projections performed by NCCD for PPS, the average inmate population will be 5,372 throughout the life of the Plan; and PPS FY95 population assumptions upon which its part of the Plan appears to be based are 5,600 in FY95 growing to 6,000 in FY99. Under the current contract, once the prison population level rises above 5,150, costs will begin escalating faster than projected in the Plan. The Prison System estimates the current population at 4,900 inmates, and PICA Staff believes it is likely that the relaxation of judicial constraints upon population levels will produce more dramatic increases than the Plan projects.

Food Service Contract — ***Upon completion of the CFCF the City will have different food service needs***

Once completed, the Curran-Fromhold facility will have a centralized food service area and improved capabilities of serving food to most of the prison population. The current annual food service contract will have to be revisited because of these changes; therefore, present projections for food costs are very speculative. Similar to health services, absent other economies food costs will increase as the prison population grows.

Preventive and Normal Maintenance — ***An adequately funded and organized preventive maintenance plan is needed to preserve the prison facilities***

Both the ten-year capital plan and the facility assessment report discuss PPS Maintenance Division deficiencies in great detail. These documents indicate that poor management and insufficient funding and staffing levels have caused the Prison System's facilities to deteriorate at a faster pace than necessary. The Prisons System has budgeted $1.3 million for repair and maintenance this year, which is a 32 percent increase over the previous fiscal year. While this increase is significant, spending projected in the Plan for this purpose levels off and may not be sufficient. PICA Staff cannot overemphasize its strong belief that an improved system is vital to keeping the new facilities in good operating order.

DEPARTMENT OF PUBLIC HEALTH

Primary Areas of PICA Concern

- o District Health Centers
  - Future Role
  - Investment Strategy
- o Local Match for Grant Funding
- o PNH Contract
- o City's Role in Managed Care for MH/MR and Drug/Alcohol Problems

Plan Expenditure Projections FY95-FY99 (millions)

	FY95	FY95-FY99
Class 100	$ 36.6	$188.9
Class 200	76.1	392.1
Class 300/400	2.4	12.1
Class 800	1.3	1.3
Total	$116.4	$594.4

Introduction

Department of Public Health (DPH) General Fund costs are projected to decrease in FY95, as they did in FY94, due to increasing recognition of grants program expenditures as an offset against grants program revenues in the Grants Revenue Fund. General Fund costs for DPH services are projected to decline from $189.8 million in FY94 to $116.4 million in FY95. The all funds expenditure total, however, is projected to increase from $420.4 million in FY94 to $604 million in FY95. A large portion of the FY95 increase is the anticipation of $140 million in entirely new funding (in the Grants Revenue Fund), for Medicaid mental health and drug and alcohol services which the City hopes to administer as a subcontractor for area HMOs. Net of the impact of anticipated new grants, the overall expenditure increase from FY94 to FY95 is approximately 10 percent.

DPH has, in recent years, substantially increased the role of outside providers in the services it delivers. Services it contracts out include activities related to substance abuse, maternal and child health, mental health and mental retardation, communicable diseases, the operation of the Philadelphia Nursing Home, Prison health services, and Riverview medical services. The latter three have been most recently privatized.

The Department maintains that it regularly reviews the services and functions it provides directly (to determine whether privatization is appropriate); that it encourages efficient contract management to ensure quality service delivery; and that it continually seeks to recover revenues that are rightfully owed to the City. In addition, DPH states that it seeks out new resources whenever possible in an effort to decrease the approximately 20 percent of total costs of service that are funded through City tax dollars.

The Department considers itself an important partner in a network of local health care providers. Its primary programmatic priority for the next five years appears to be the revitalization of the District Health Centers. Areas of focus include an automated scheduling system; the ability to serve "walk-in" patients in a timely manner; active outreach for potential patients; active solicitation of managed care plan relationships; improvement of physical conditions at the Centers (including a multi-year capital rehabilitation plan for facilities); and improvements in DPH's ability to attract and retain competent contract physicians in a changing health care environment.

Strategic Planning for District Health Centers -- *As national health care reform looms on the horizon and a transition to managed care occurs, the full range of options for the future role of District Health Centers should be considered*

While only 5.7 percent, or $24.1 million, of the Department's total FY94 projected expenditures were for the District Health Centers Division, 16.8 percent, or $14.3 million, of the Department's unreimbursed obligations were incurred in the Division's operations (this includes allocating County Health Act revenue as reimbursements for the District Health Centers, a conservative methodology which is not totally realistic since those dollars could alternatively be applied to many of the Department's other activities under the provisions of the County Health Act).

The Department has indicated that in evaluating what the strategic response of its District Health Center system to the probable transition to an HMO-based public health system should be, four options have been considered: (1) maintaining the *status quo*; (2) becoming a preferred provider for selected managed care organizations; (3) seeking partners with whom to become a competitive managed care organization; and (4) becoming an HMO and competing as a primary bidder to provide service. These options are currently useful to the extent that they will enable the City to continue serving the Medicaid-insured population (as Medicaid services will in the near future be primarily provided though HMOs). The City has chosen option two, for the short term, as being the most feasible option to maintain the ability to serve Medicaid patients and receive reasonable reimbursements. In addition, the City has formed an unincorporated association with other federally funded health centers in the City to expand its options in a managed care environment.

Nonetheless, PICA Staff is concerned that the Department's analysis of how best to respond to the Medicaid managed care challenge and other changed conditions does not adequately address the long-term question of the possible role of the Health Centers in the event of national health care reform legislation (or otherwise). The City has articulated the basic mission of the District Health Centers as serving as a safety net for the uninsured population of the City.

In the opinion of PICA Staff, if Federal health care reform provides for universal health care, this mission will no longer exist, and the Health Centers will be required to consider options such as shutting down or filling the gaps which remain in the safety net. If universal health care does not come into effect, or falls short of insuring everyone, the basic mission will remain, and the question will be how to accomplish it most cost-effectively. Direct services, contracting out, and requiring services in lieu of taxes from not-for-profit health care providers, should be among the options considered. The Plan states that the District Health Centers will "inevitably" continue to be a major health provider network. PICA Staff finds it difficult to accept such an "inevitability". If the private sector finds it profitable to provide services previously provided by the public sector (because of a new Federal health care program or otherwise), and the City can save money by no longer being the service provider of last resort while ensuring quality of care, then the continuity of the function should be carefully evaluated, and plans for physical plant improvements judiciously reviewed. PICA Staff, in response to questions, was advised by DPH that it had not done any cost-benefit analysis on alternatives to the City continuing as a direct provider of services, nor did it intend to do so.

A departmental initiative to evaluate District Health Center financing through a consultant team is underway; recommendations are anticipated in FY95, but no impact has been assumed in the budget for FY95. PICA Staff anticipates reviewing the results of this analysis when it becomes available.

District Health Centers -- *Substantial incremental capital investments are being made without benefit of a strategic plan*

The Department has various initiatives underway to improve the efficiency of the Health Centers, including initiatives to improve customer service regarding scheduling of appointments; to timely serve "walk-in" patients; and to enhance the City's ability to attract and retain competent physicians through competitive compensation packages. In addition, the operating budget includes increased appropriations of $1 million and increased staff (20 full-time positions, including six coordinators, two maintenance mechanics, nine clerical personnel, one HVAC mechanic, one painter and one pharmacist). The City's FY1995-FY2000 Capital Program includes over $5 million for Health Center rehabilitation. Yet the Department is only now conducting a review of staffing patterns, doctor-patient ratios, and support systems to ascertain the overall effectiveness of the Centers. PICA Staff considers it problematic that significant new investment is being made prior to such basic reviews being completed. It is not clear how incremental funding decisions can be made intelligently without these reviews in hand to provide guidance.

Initiatives aimed at increasing revenue at the Health Centers have had a measure of success. Revenue is projected to increase significantly in FY94 with small additional increases during FY95 through FY99. Much of the increased revenue at the health centers was the result of attaining Federally Qualified Health Center status, which has allowed the City to qualify for a higher reimbursement rate per visit for visits covered under Medicaid. The estimated increase in revenue as a result of this initiative is $1.3 million in FY94. Another major factor was increased reimbursements from HMOs (which appear to be due to a large increase in the number of visits covered by HMOs). Some revenue enhancement initiatives, such as increased revenue from privately insured patients and increases in the percentage of billings collected, have not been realized.

Local Match for Grant Funding -- *There could be a major local matching requirement impact in prospective grant programs*

DPH obligations from FY85 to FY93 increased an average of 10.7 percent annually. Departmental revenues increased even more rapidly, at 11.9 percent. As a result, unreimbursed obligations increased at 7 percent annually, well below the rate of increase in overall expenditures. Unreimbursed obligations formed a decreasing percentage of total obligations during the period, declining from 28.3 percent to 21.6 percent. While it makes sense to increase local health funding in order to leverage even larger increased in Federal and State funding, PICA Staff is concerned that unreimbursed obligations are increasing faster than the tax base. In addition, eventually the increase in intergovernmental revenues may slow or reverse, leaving the City with a high level of service expectations which it will be difficult to reduce, regardless of the availability of funding.

The Department has budgeted a 25.9 percent increase in reimbursement in FY94. The FY95 budget projects an increase of 11.5 percent. MH/MR spending in the Grants Revenue Fund and General Fund combined, not including the managed care grant which is an entirely new source of projected funding in FY95, is projected to increase 6.7 percent in FY95, following a 12.2 percent increase in FY94. PICA Staff continues to have a concern that such large increases in grant funding might adversely impact the City's ability to provide future local matching requirements for these grants, and saddle it with ongoing financial responsibilities after grant funding ceases.

Philadelphia Nursing Home Contract--*Concerns exist about performance monitoring, and the process of passing Medicaid and Medicare revenues through to the operator*

The City contracted out the operation and management of the Philadelphia Nursing Home to Episcopal Hospital, beginning January 31, 1994.

It is vital that adequate resources be devoted to the City's management of this important contract. The City has provided for one contract monitor and one patient care coordinator in FY95. There is an underlying concern on the part of PICA Staff as to whether this is a sufficient contract management staff, particularly since the Plan states that insufficient monitoring could result in increases in the City subsidy to Episcopal Hospital.

There is also a concern as to whether the Plan's Class 200 growth assumptions for DPH are consistent with assumptions about growth in PNH revenue (which is passed through the City budget and relates to PNH Class 200 expenditures). The FY95 budget also includes $1.3 million in Class 800 expenditures for PNH, which is a pass-through of Medicaid capital funding. No Class 800 expenditures are included for PNH after FY95. At the same time, overall Medicaid PNH revenues are projected to grow 4.7 percent from FY95 to FY96, which suggests that the non-capital portions of Medicaid will grow by 9.3 percent. By contrast, the Plan growth in Class 200 for DPH is 1.5 percent in FY96. To make up this difference, the growth rates for other DPH Class 200 items would have to be very low. These items include prison health care, which is based on a fixed price plus an additional $2.20 for every inmate above 5,150, and this could grow if the prison population increases, as is projected elsewhere in the Plan.

Managed Care for Mental Health and Drug and Alcohol Program Services --
Financial implications of the City's contemplated role are not clear

The City has budgeted $140 million in the Grants Revenue Fund in FY95 for the initiation of an Administrative Service Unit which will operate a mental health/substance abuse managed care network. This is an initiative whereby the City would administer the MH/MR and drug and alcohol portion of the Medicaid program within the City on subcontracts from HMOs. This is DPH's response to the State Health Choices program, under which all medical assistance-eligible Philadelphia residents are to receive services through HMOs under contract with DPW. Under the Health Choices program, Medicaid recipients will be allowed to choose one of a handful of HMOs, or be assigned an HMO if no choice is made. The claimed advantage of DPH administration is that the City already administers a substantial mental health/drug and alcohol program, and therefore has the incentive and knowledge to make cost effective decisions and maximize Federal funding. The potential disadvantage is that such service could expand the City's financial support roles in these programs, with resultant costs. Another problem is that many of the HMOs are regional and may not be interested in negotiating separate contracts with individual counties.

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DEPARTMENT OF PUBLIC PROPERTY

Primary Areas of PICA Concern

- o Utility Savings Projected from Initiatives
- o Space Rental Costs
- o City Share of SEPTA Subsidy Projected to Decline
- o Consolidation of Building Services

Plan Expenditure Projections FY95-FY99 (millions)

	FY95	FY95-FY99
Public Property	$ 40.0	$205.9
SEPTA Subsidy	49.1	271.5
Space Rentals	28.3	104.1
Utilities	45.3	217.9
Vehicle Leasing	9.1	19.8
Total	$171.7	$819.2

Introduction

The Department of Public Property (DPP) is responsible for a variety of internal services provided to other City departments, including space rental and planning; construction, renovation and maintenance of buildings; custodial services; and telephone and utility payments.

Utility Costs -- *Ambitious cost reductions are projected as a result of initiatives*

Utility costs are projected to increase 13.3 percent in FY95, decline in FY96 and FY97, and increase a minimal amount in FY98-FY99. While there is a significant increase in FY95, from FY95 to FY99 there is an average annual decrease of 1 percent, which is a significant difference from previous plans. The FY92-FY96 Plan projected 6.5 percent annual increases, while the FY94-FY99 Plan projected 2 percent annual increases.

The reason for the difference is twofold. The current Plan assumes $16 million in savings from initiatives undertaken by the Municipal Energy Office (MEO) which were not projected in previous Plans. In addition, the initiatives positively impact a base cost projection, which increases more slowly than in previous Plans' projections. The base cost projection in the FY95-FY99 Plan shows a 1 percent average annual increase from FY95 to FY99, well below the level of increase projected in previous Plans, and below the Plan's 3.5 percent projected inflation rate.

MEO was established in July 1993 to coordinate energy conservation efforts and improve energy-related procurement. There are ten separate MEO initiatives which together result in a projected $4.2 million in annual savings in energy costs. It is not clear to what degree savings estimates have been discounted in order that shortfalls in some initiatives can be balanced out against additional savings from other initiatives.

This is a concern since most of these initiatives are still in the early stages of implementation or are still being analyzed.

One of the initiatives, the "Aladdin project", funded by the Productivity Bank, is an energy efficient bulb replacement program. This initiative is the source of a projected $2.6 million in utility savings over the Plan, but as of January 31 has produced FY94 savings of only $22,000, compared to an originally projected savings of $374,000 in FY94.

The largest projected savings, $1.1 million annually, come from an initiative to replace existing traffic signals with LED signals. This project is currently being piloted, and financing for a citywide expansion is being sought. Other initiatives involve projects at Health and Library facilities, Veterans Stadium and the Art Museum.

The prospects for MEO achieving quantifiable success will be hampered by many City facilities not having independently metered electrical power sources, particularly for street, alley and traffic lights. This is one area where the deficiencies in the City's cost allocation system make projections suspect.

Space Rentals -- *Rental costs are projected to decline as a result of reoccupying the Municipal Services Building, but little additional savings are projected*

Space rental costs are projected to decline from their FY94 level of $29.2 million by 3.4 percent in FY95, 22.6 percent in FY96, and 18.7 percent in FY97. After that costs increase 2.8 percent in FY98 and decrease 2.2 percent in FY99. The total contemplated reduction from FY95 to FY99 is $10.4 million. This reduction can be almost entirely accounted for by the elimination of the $9.8 million FY95 rent projected for 1600/1650 Arch Street, which will occur when the City vacates its temporary occupancy of those buildings to return to the renovated Municipal Services Building (MSB). There appears to be little additional net savings projected in the Plan beyond that attributed to the re-occupancy of the MSB.

Given the potential for relocation of some City offices into the space vacated by the Courts when they occupy the new Criminal Justice Center (CJC), as well as the continued softness of Center City real estate rental market, it seems that additional savings may be possible in the space rental budget.

Space planning could assist the Department to capitalize on opportunities for savings. DPP has long been in the process of drafting a long-term space plan for City departments, to address issues such as the return of City departments to MSB, the transfer of court offices to the new CJC and reuse options for City Hall. The space plan, which has been long delayed, was recently projected to be complete in April 1994, although the current estimates expect finalization during the first quarter of

FY95. Given the projected movement of activities to the MSB and CJC, as well as the potential for the City to enter into long-term real estate leases, the need for a space plan is obvious.

SEPTA Subsidy -- ***The Plan assumes increases in the suburban share of the local operating subsidy***

SEPTA receives a local government operating subsidy equal to one-third of the annual State operating subsidy. The City is currently responsible for funding 70 percent of the local government operating subsidy, while the suburban counties in SEPTA's operating area are responsible for the remaining 30 percent. The City is in the process of discussing reallocation of the local SEPTA operating subsidy with the suburban counties. The Plan assumes a reduction in the City share to a level between 50 and 60 percent of the local subsidy by FY97, a level which is assumed to last through FY99.

The overall City subsidy to SEPTA in the Plan is projected to decline in FY95 and grow at 5 percent annually in FY96-FY99. The State budget projects a 3 percent increase in mass transportation assistance in FY95, which suggests that the FY95 Plan projection could be too low absent some immediate reduction in the City share of the local operating subsidy.

Factors that could adversely affect the SEPTA subsidy projection in the Plan are reductions in the Federal operating subsidy, declining ridership, and difficulty in achieving the projected reduction in the City's share of the local subsidy. The City, in making the assumption about the changes in subsidy formulas, is pressing the limits of the PICA Act. The statute anticipates that deviations from existing law may be incorporated into the Plan only in limited circumstances, and no information has been provided that supports the underlying change in assumptions.

Consolidation of Building Services -- ***It is appropriate that City plans to devote attention to facility maintenance, but additional funding may be needed***

During FY95, the Administration has indicated that it plans to consolidate building services functions. Such a consolidation, combined with the development of a computerized facility management system, has the potential to achieve economies of scale, improve building services quality and provide a more rational basis for exploring the cost-effectiveness of contracting out certain services. It may also help to improve the City's decision making concerning the most cost-beneficial levels of investment in preventative maintenance.

It is the hope of PICA Staff that if a central office for facility management is established, the City will fund the needed level of ongoing facility maintenance. With the recent expansion in the capital program, it is appropriate that the City devote additional attention to the maintenance of the facilities in which it is investing millions of dollars. The City has budgeted small increases in FY95 for building maintenance in the Recreation Department and the Free Library, and in DPP, which is responsible for maintenance of Police and Fire Department facilities. PICA Staff's concern is that additional funding increases are probably needed over the course of the Plan to bring the City to a level of commitment where recent investments in facilities can be maintained. The Plan does not appear to budget for a significantly larger maintenance commitment during the FY96-FY99 period, and while consolidation of effort may produce economies which can be used for the benefit of facilities, no plan to accomplish that goal has been shared with PICA to date.

REVENUE AND LAW DEPARTMENTS

Primary Areas of PICA Concern

- o Maintaining High Rates of Law Department Collections
- o Implementation of TIPS System
- o Diminishing Returns for Additional Collections Initiative
- o Alternatives to Suburban Withholding

Computerized Collections Initiative
FY94 Revenue Projections
(millions)

Project	Plan*	Current
Integrated Tax System	$3.0	$0.33
Real Estate Tax System	1.5	0.00
Earnings Tax System	1.0	0.47
Automated Audit System	.0	0.37
Total	$5.5	$1.17
Shortfall		78.2%

*FY94-FY98 Plan

Introduction

The Revenue and Law Departments are discussed together since they have several jointly managed initiatives.

Within the Revenue and Law Departments there are three major groups of initiatives to increase revenues, in the form of the Revenue Department's Computerized Collections and Additional Collections initiatives, and the Law Department's Collections initiatives. These three groups of initiatives are projected in the Plan to produce over $25 million in City revenues in FY94. A significant amount of the City's tax revenue growth since FY92 has been due to the impact of Law and Revenue initiatives, as the growth in collections of prior City taxes has far outpaced the growth in current levy collections. Thus, projecting the future progress of these initiatives accurately is a key element in projecting the City's overall revenues.

The Plan does not separate growth of revenues from the Law and Revenue Department initiatives from growth due to other factors (with the exception of revenues from the Tax Review Board Acceleration initiative). Knowing the different effects of each initiative is important to the accurate projection of overall City revenues, and it would be helpful to analysts were the City to state these effects in its revenue projections.

Law Department

Law Department Collections -- ***Revenues are meeting budgeted targets, but success in reaching future targets depends on continued referrals from the Revenue Department, which may diminish as the backlog of delinquent taxpayers is reduced***

The Law Department has increased its tax collections significantly since FY91. Collections through the first six months of FY91 were $20.4 million. During the same period in FY94, they were $31.1 million. The Department attributes this improvement to the combined effect of computerization of the Department's Enforcement Unit and the hiring of 15 additional staff in the Unit.

The anticipated impact in FY94 is measured in terms of the increase of collections over FY91 levels, and is projected at $20.3 million. Accordingly, the Department must collect an amount $9.5 million above the amount collected in FY91 during the final six months of FY94, in order to meet its revenue projection for the initiative.

Despite the positive results to date, the Law Department recognizes that at some point additional revenues from this initiative will decline, due to decreasing numbers of cases and fewer referrals of delinquent tax cases from the Revenue Department. The Law Department is involved in discussions with the Revenue Department to assure that referrals will continue at a rate sufficient to actuate anticipated revenue. Delays in the computerization initiatives in the Revenue Department may adversely affect referrals. A related concern for the Law Department is the acquisition of capability (hardware and software) to access MOIS and other departmental data bases, allow the immediate transfer of information from the Revenue to the Law Department, and permit the Law Department to manage its caseload efficiently. It is important that these links be forged, in order that the Law Department can benefit from TIPS, the Revenue Department's integrated database of taxpayer records, as it is implemented.

One PICA Staff concern is that the Law Department's reporting of collections does not distinguish revenues according to whether the collections are current taxes or prior years' taxes. This makes it difficult to determine the degree to which growth in City taxes is the result of growth in the tax base, or how much is the result of increased enforcement.

Revenue Department

Computerized Collections -- *The project has had difficulty meeting its implementation schedules, and revenue projections continue to be revised downward as a result*

There has been a continued downward trend in projections of revenues from this initiative, as the implementation timetable has continued to slip. The initial FY94 projection for computerized collections, contained in the FY94-FY98 Plan, was $5.5 million. The current FY94 projection for these initiatives is $1.17 million, a reduction of 78.2 percent. FY93 revenue projections also were revised downward during that fiscal year due to implementation schedule slippage.

The Computerized Collections initiative will significantly change the City's approach to enforcing its tax laws, if it ultimately is successful in fulfilling its promised capabilities and if the Department allocates other resources (both financial and managerial) needed to optimize its potential. While revenue impacts from this initiative to date have been small compared to other revenue initiatives, they are projected to increase significantly in the future. TIPS is to allow the Department to match taxpayer records both within the system (with respect to different taxes owed by the same taxpayer) and with records maintained by the Pennsylvania Department of Revenue and the U.S. Internal Revenue Service. Internal matching will allow audit and enforcement activities for different City taxes to be carried out in an integrated manner (*i. e.*, different tax units will not pursue the same taxpayer separately for different taxes owed). External matching will enable increased discoveries of taxpayer deficiencies and joint enforcement with the State and Federal governments. $11.5 million in additional General Fund revenues are projected from TIPS in the FY94 to FY99 period. The City also projects additional revenue benefits for the School District and the Water Fund.

The City intends to integrate its various tax systems into TIPS. Self-assessed taxes, including the Business Privilege Tax and Wage Tax, are to be incorporated into TIPS by May 1994. Other tax systems, such as the Earnings, School Income, Use and Occupancy, Real Estate, Personal Property and the water billing system, are to be integrated gradually through November 1995. Through 1996 and 1997, the Department expects to make progress toward consolidated taxpayer accounting, billing and posting.

Proceeding concurrently with the integration of tax systems into TIPS, the discovery program will consist of four phases: audit systems I and II (projected to be completed in June 1994); external matching with IRS data for the Earnings Tax (reported as complete in March 1994); internal matching across City tax types (to be completed June 1996); and external matching with State and IRS data (to be completed March 1997).

Also, beginning in January 1996, returns creation and processing are to be automated, and an imaging capability is to be created for data capture, storage, and retrieval, which is to be completed by December 1997.

Key preconditions for the success of TIPS will be the ability of the Department to reorganize staff, reengineer processes and redefine job descriptions to support the system properly.

There are three additional elements to the Computerized Collections initiative: the automated audit system, the Earnings Tax System, and the Real Estate Tax system. The Department will replace current manual auditing procedures with an automated audit system that is intended to improve audit selection, detect discrepancies on returns and accelerate taxpayer notification and billing. Collections of $4.3 million from this initiative are projected over the Plan, based on the following assumptions: the audit assessment base level, $13,913,000 in FY92, will increase in FY94 to a level 3 percent higher than the base level, 8 percent above base levels in FY95 and 10 percent in FY96. No additional increases are projected in FY97 and FY98. Based on historical patterns, collection increases are projected at 80 percent of increased assessments.

The Earnings Tax is levied on earned income of persons with respect to whom Wage Tax is not withheld by an employer (including residents employed outside Philadelphia and non-residents employed within Philadelphia). According to the Revenue Department, its Earnings Tax System initiative intends to increase Earnings Tax collections by permitting the Department to utilize Pennsylvania Department of Revenue and IRS data fully to support additional discovery of non-registered individuals who are subject to the Earnings Tax. $4.2 million in additional revenues are projected from this initiative from FY94 to FY98, with $469,000 in FY94. The revenue projections were based on the percentage increase in revenues achieved from implementation of a similar initiative with respect to the School District Unearned Income Tax in FY87. The percentages were reduced from those achieved in the case of the School District, according to the City, to reflect currently weaker economic conditions. The City recently sent billings of $11 million to taxpayers who were determined to owe Earnings Tax based on an examination of 1989 Federal tax returns.

The Real Estate Tax System is to promote timely and accurate billing of accounts receivable, increased billing frequencies and more timely and effective enforcement actions. $7.5 million in additional General Fund revenue is projected from FY95 to FY98. Additional revenues are expected to be generated for the School District.

Additional Collections Initiative -- *Collections are well over FY94 budget amounts, but are down from FY93 levels*

The FY94 projection of revenues to be received from the Additional Collections initiative is currently in excess of $10 million. The FY94 budget contemplated receiving $6 million from this initiative. Nonetheless, FY94 projected revenues from additional collections are significantly below FY93 collections of $13.8 million. This is the result of a reduction in the backlog of delinquent cases, and further reductions are likely as the backlog continues to be reduced.

The Additional Collections initiative includes four parts:

The Discovery Project involves the discovery of non-filers by Law Department co-counsel. The Department originally anticipated $3.5 million in FY94 revenue, and is currently projecting $6.4 million.

The Return Mail Project attempts to locate real estate taxpayers for whom the Department does not have an accurate mailing address. The benefits from this project are expected to decrease with the implementation of TIPS, which should improve name and address identification. Benefits were originally anticipated at $1.5 million in FY94, and are currently projected at $1.8 million.

The Tax Review Board project increases collections of delinquent Earnings and Business Privilege Taxes by offering partial interest and penalty relief for cases under appeal to the Tax Review Board. Benefits from this initiative were originally anticipated at $1 million in FY94, and are currently projected at $1.4 million.

The Audit Project consists of an offer of a partial waiver of interest and penalty charges to recent auditees in return for immediate payment of all remaining liabilities. Revenue benefits in FY94 are projected at $340,000.

Suburban Withholding -- *Enabling legislation is still awaiting legislative approval, while other avenues are pursued*

Another major initiative in the Revenue Department is suburban withholding. The original projection was that $9 million in FY94 revenue would be raised from this initiative. Enabling legislation has not been passed by the General Assembly. Many of the goals of this initiative are likely to be achieved through the TIPS system, but the timetable for implementation may be considerably longer with this approach.

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STREETS

Primary Areas of PICA Concern
o Sufficient Vehicle Availability
o Street Cleaning Modernization Delay
o Communications System Delay
o Snow Removal Costs
o Personnel Cost Projections

Plan Expenditure Projections FY95 - FY99 (millions)

	FY95	FY95-FY99
Class 100	$ 55.8	$284.3
Class 200	68.1	350.7
Other	2.9	13.2
Total	$126.8	$648.2

Introduction

The mission of the Department of Streets is to provide functionally clean and safe streets in a cost-effective and efficient manner for all who live, work, and visit in the City of Philadelphia. The Department has five divisions, with the two primary units being Sanitation and Highways. Sanitation, the largest, comprises in excess of 75 percent of the overall departmental budget.

The Plan projects that the Department's FY95 obligations will decrease by $21.8 million (14.7 percent) from FY94. This reduction is the result of lower cost waste disposal contracts and the expected closing of a trash transfer station. The Department's total obligations are projected to grow 1.1 percent in FY96, 1.4 percent in FY97 and then less than 1 percent annually in FY98 and FY99. The Department's cumulative Plan obligations are projected to be $648.2 million. The Department, to deliver its services at the projected funding levels, must improve efficiency and take advantage of the latest available technology.

Waste removal is the Department's largest "purchase of service" (Class 200) cost, and the Department has a history of anticipating the removal of more waste tonnage than it actually handles. The Department has indicated that original FY94 tonnage projections were utilized as a base in the formula used to calculate tonnage costs for the Plan. FY94 costs are currently 3 percent below those originally projected. Unless the growth rate increases appreciably, the ultimate costs of waste disposal should be lower than the Plan's projections.

Departmental Strategic Plan

To become more efficient and develop a better understanding of its future, a Streets Department task force in 1993 developed a departmental strategic plan which addressed the Department's missions, goals, strategies, and tactics for the FY94 - FY98 period. The following goals were established for the Department:

Solid Waste Management -- This section follows the revised guidelines in the City's Municipal Waste Management Plan adopted by City Council in 1991. The waste management plan established guidelines to improve solid waste collection services, encourage waste minimization, expand and improve recycling and promote environmentally sound solid waste management practices. To adhere to these guidelines, the Department developed new procedures for:

- o Collection Efficiency -- The Sanitation Division now emphasizes the use of training, improved management techniques, and technologically advanced equipment as keys to efficiency improvement;

- o Waste Minimization -- Through programs such as increased recycling and customer education (including in-school programs), the Department attempts to reduce the amount of solid waste it must process;

- o Recycling -- Through marketing efforts for an expanded recycling market, the Department seeks to maximize the amount of waste which can be returned to beneficial use; and

- o Disposal -- The Department continues to balance the use of its disposal contracts in a manner which is intended to yield the greatest efficiencies over the combined collection and disposal systems.

The Department plans to purchase additional 20 cubic yard compactors to increase collection efficiency, increase the neighborhoods participating in mandatory recycling for waste minimization, and close another transfer station.

Street Cleaning -- Clean streets in both commercial and residential sections of the City has been an historical problem. With the opening of the Pennsylvania Convention Center the cleanliness of Center City streets becomes more important. The Market Street East project and the Center City District (CCD) have done much to assist in alleviating center city street cleaning problems. PICA Staff was disappointed to note that the CCD, in a recent newsletter, indicated the City has not regularly fulfilled its commitment to the District to empty corner trash cans two to three times daily or to mechanically sweep the streets daily.

The Department indicates it has focused on the following areas:

- o Education -- With the help of the School District, the Parochial School system and the media, the Department is attempting to make citizens aware of their responsibilities and ways in which they can help the Department meet its responsibilities to maintain a clean city. It has initiated a program that is marketed through PhilaPride which supports the education and clean-up program through a "junior block captain" initiative.

- o Enforcement -- The Department has initiated an expanded city-wide sanitation enforcement program in the commercial business areas and neighborhoods.

- o Performance -- The Department has represented that it will implement new cleaning schedules that are better tailored to the cleaning needs of the area.

PICA Staff believes that the development of a departmental strategic plan indicates the Department's willingness to restructure in order to make an effort to better perform its mission, although to be successful over the long-term it must be linked to both clearly defined output standards and the Citywide strategic planning process. PICA Staff concerns relative to Plan-projected savings that are to result from the Department's strategic plan-devised goals, because of initiative delays or other restrictions, are discussed below.

Curbside Collections -- *It is important that progress continue in improving service delivery*

The Department's ability to collect trash efficiently is dependent on the continued availability of sufficient vehicles, implementation of tonnage standards for crews, a more rational approach to routing, continued replacement of older vehicles with high density compactors and reductions in absenteeism. The combination of improvements in each of these areas would greatly enhance the Department's ability to collect trash on-time while minimizing overtime costs.

Sufficient Vehicle Availability -- *While the number of Streets Department vehicles available on a regular basis has vastly improved, it is still below established requirements*

In order to operate most efficiently, the Streets Department has indicated a need to have 220 fully operational vehicles in service each day. While the Department acknowledges that vehicle availability has improved markedly since the creation of the Office of Fleet Management, the available number generally remains below the Department's requirements. The Streets Department has reported to PICA Staff that daily vehicle availability currently averages around 200. A continuing lack of the appropriate number of operational vehicles could negatively affect the Plan.

Street Cleaning Modernization Delay -- *There have been litigation delays for the Street Cleaning Modernization initiative*

The goal of this initiative is to convert the cleaning function on many Center City and neighborhood commercial streets from manual to mechanical processes. The City anticipated savings from this initiative through attrition, however the union opposed changes to replace previously staffed block cart routes. The union successfully appealed this change. As a result, the City will be required to restore sixteen block cart operators to its budget as part of an as-yet incomplete agreement with labor unions concerning Center City cleaning. The Department has estimated the additional annual costs to be $400,000 to $500,000.

The Department indicated that the Plan was built on the assumption that additional mechanical brooms would be put in service by July 1, 1994. The Department since has provided information to the Authority to the effect that delivery of the mechanical brooms has been delayed and it is now anticipated that their use will be phased in over the first half of FY95, with two expected in August, two in the Fall, and the final two in December. This delay will negatively affect its FY95 service delivery capacity.

Communications System Delay -- *The Streets Department has indicated that the 800 MHz communications system is two years behind schedule*

In an effort to make the Sanitation and Highway Divisions more efficient, the Department is developing a Geographic Information System (GIS). This system, among other things, will aid in the development of better routes and work schedules intended to reduce overtime and improve customer service. The Streets Department received a $1.2 million loan from the Productivity Bank to develop and implement the computerized routing system portion of the GIS. Annual savings from implementing this initiative, projected to be $419,000, were to be utilized to reimburse the Productivity Bank. The Department emphasized that the overall project savings were dependent upon access to a new Department of Public Property-acquired 800MHz radio system, which would allow all personnel to communicate quickly and efficiently.

In the Monthly/Quarterly Status Report dated January 10, 1994 the Streets Department indicated that, as a result of delays in procurement of the new radio system, full implementation of the computerized routing system may be delayed for up to two years. The Department has stated that 400MHz radios will serve a portion of its fleet in the interim. The Department has indicated that this will reduce projected savings in FY94 through FY96 and also effect the Department's ability to reimburse the Productivity Bank as scheduled.

The communication system's delay will negatively affect several areas within the Streets Department. In Council testimony the Department indicated it planned to expand the GIS system in several areas (such as to create a pavement management system and compile a street lighting and traffic infrastructure inventory) to generate further savings. Streets Department strategic plan's progress also will be impacted. Historically, the Department has been criticized for an antiquated route mapping system, and resultant poor scheduling practices which contribute to increased costs and inefficiencies. The Department's goal was to correct this situation utilizing components of the GIS coupled with a state of the art communications system. The Streets Department has indicated that due to communications system delays it will be unable to initiate all of the structural changes contemplated in the Department's strategic plan on a timely basis.

Snow Removal Costs -- ***Several severe winter storms have caused the Department to spend much more than it expected for overtime costs and road salt***

As a result of an unusually severe winter, the Streets Department has had higher than projected costs for both overtime and road salt. The Department has stated that the overage will be funded with mostly Class 200, and some Class 100, savings from other divisions within the Department. In another weather-related matter, the Department is repairing an unusually large number of potholes, and total costs have yet to be tallied. The City plans to seek Federal disaster aid to defray some of the unbudgeted costs. While the City received $908,000 from the Federal government in FY94 for storm-related damage suffered in FY93, and the Federal government has issued a disaster declaration as a result of this year's storms, there can be no assurance that a similar payment will be received. PICA Staff will continue to monitor this area.

Personnel Cost Projections -- ***The Streets Department is very optimistic to project no Class 100 growth in the out-years of the Plan***

The Streets Department portion of the Plan assumes no growth in Class 100 spending for FY98 And FY99. While it may be the City's consistent policy to assume no across-the-board pay raises in FY98 and FY99, it is nonetheless appropriate to recognize the other factors that could cause Class 100 costs to rise (such as overtime and incidental pay increases). The Streets Department faces problems in controlling overtime costs, especially with the primary initiatives to control overtime (GIS, route organization and better crew management) all adversely impacted in at least some degree by the delay in the 800MHz radio system. While zero growth is not impossible for the Department to achieve, PICA Staff considers it extremely unlikely that personnel costs will remain flat unless all initiatives are successfully implemented and no extraordinary events occur.

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OFFICE OF FLEET MANAGEMENT

Primary Areas of PICA Concern

- o Vehicle Utilization
- o Overtime Costs
- o Centralized Maintenance Facility
- o Prison Vehicle Maintenance Facility

Plan Expenditure Projections FY95 - FY99 (millions)

	FY95	FY95-FY99
Class 100	$17.25	$ 88.76
Class 200	3.99	20.21
Class 300	13.89	67.92
Class 400	16.93	86.93
Class 800	.72	1.84
Total	$52.78	$265.66

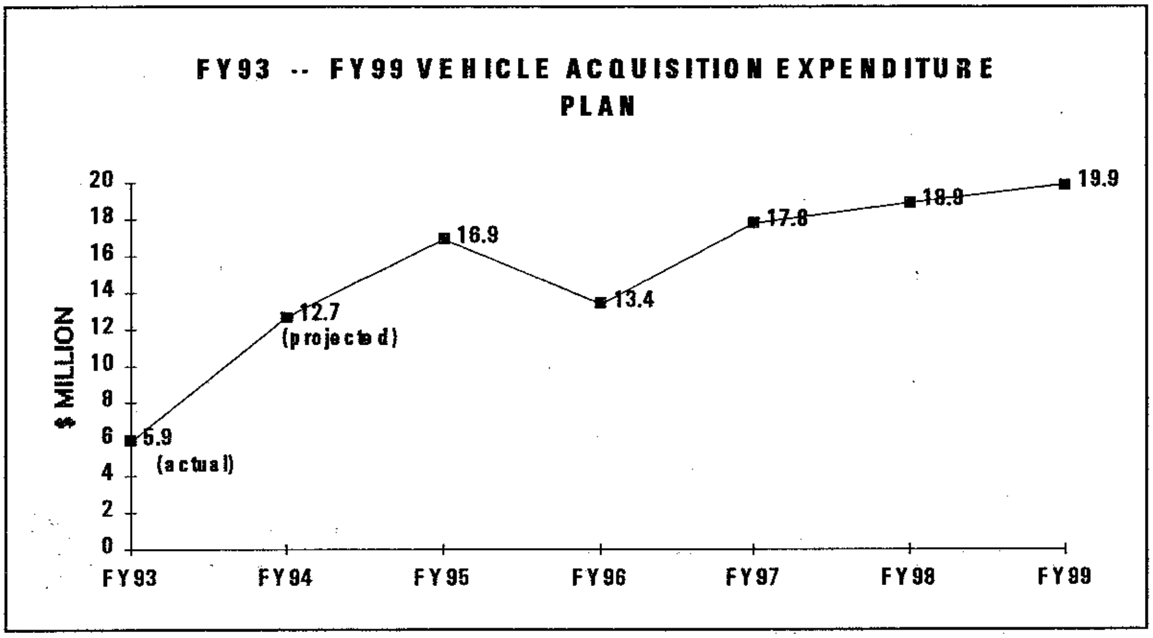
Introduction

The City hired a professional fleet manager in November, 1992 and established the Office of Fleet Management (OFM) in July, 1993. OFM was created as a direct result of recommendations made by the Mayor's Private Sector Task Force; its mission is to maintain, assign and replace the City's diverse fleet of nearly 6,000 vehicles. OFM consolidated 550 persons previously budgeted among eight City departments into a cohesive operation. As noted elsewhere in the Staff Report, the ultimate goal of OFM is to ensure that adequate numbers of appropriate vehicles are available for departments on a predictable basis. PICA Staff recommends that the City include vehicle availability data in the Monthly City Manager's Report, as it now does with overtime.

FY99 OFM-projected total obligations (excluding vehicle acquisition) total $4.2 million less than the Plan's FY94 projected obligations. The major reason for this decrease occurs in FY95 when budgetary responsibility for Water Department fleet operations is shifted to the Water Fund. This transfer totals $6.9 million, allocated to Class 100 ($1.8 million), Class 200 ($3.2 million) and Class 300 ($1.9 million).

OFM obligations for other than vehicle acquisition show little growth throughout the life of the Plan. Class 100 expenditures increase $346,100 (2 percent) and $379,200 (2.1 percent) in FY96 and FY97, respectively, while overall expenditures are projected at a slight decrease after projected repayment of the Productivity Bank loan in FY95 through FY97. FY99 projected expenditures, in total, increase only $3,808 over FY95 projections.

The Office of Fleet Management's projected vehicle acquisition expenditures (Class 400) are substantial over the life of the Plan, a dramatic change from the recent past when the vehicle acquisition program was reduced as a budget balancing measure. The Plan seeks to correct the adverse impact the City's aged and poorly maintained fleet has on its ability to operate efficiently. OFM is conducting a zero-base analysis with all departments to determine optimum fleet size and specific vehicle needs. The following chart depicts the resulting vehicle acquisition expenditure plan:



This graph shows that vehicle purchase expenditures are projected to increase $4.2 million (33 percent) in FY95, then decrease by $3.5 million (21 percent) in FY96 and thereafter grow by approximately $1 million annually over the FY95 level throughout the remainder of the Plan. PICA Staff is pleased to see OFM's commitment to modernize the City's fleet, and is cautiously optimistic as to its ability to maintain the new fleet properly.

Vehicle Utilization -- ***Proper vehicle utilization is singularly important to successful fleet operations***

The Plan states, and PICA Staff agrees, that "the new preventive maintenance program developed and implemented by OFM is probably its single most important initiative to date." Historically the City's vehicle operators were reluctant to deliver vehicles for preventive and normal maintenance because systemic weaknesses were productive of scheduling delays and long down time. To help to combat this problem OFM purchased a computer data base known as the "fleet accounting computer tracking system" (FACTS) to establish, and notify departments of, regular maintenance schedules. FACTS has the ability to cut off a user's "City gas" supply if vehicle operators do not adhere to proper schedules. As well, the system has the capacity to provide information to departments to help them understand that the lack of attention to maintenance will over time adversely effect the ability of the agency to do its job.

Another area of concern to OFM is the problem of "high risk operators". OFM has indicated that it will track and identify drivers who consistently abuse their City vehicles. OFM has yet to establish a system that will effectively deter abuse or limit future vehicle privileges of abusive users. PICA Staff believes that until this area is addressed, in combination with FACTS making departments and drivers more aware of their responsibilities, preventive maintenance operations will continue to be hampered.

Overtime Costs -- ***Overtime costs for the Office of Fleet Management continue to far exceed budgeted levels***

The Monthly City Managers Report for the month ending February 28, 1994 projects OFM FY94 overtime costs at $2.7 million, $1.7 million (149 percent) over its original budget. OFM has indicated that the primary factors contributing to the overtime problem are a continued backlog of necessary initial maintenance tasks and the unusual additional work resulting from the extraordinarily harsh winter. Overtime for OFM is expected to continue to grow because storm-related vehicle problems continue to surface and all costs have yet to be accounted for.

The City also has indicated that overtime costs for OFM are difficult to budget because its comprehensive programs are relatively new and no historic spending patterns are available to make accurate projections. While both the accumulated backlog and harsh winter may have been events peculiar to FY94, and it is understandable that a new organization has no historic data on which to base its projections, overtime could readily continue to be a problem area in the Plan's later years. Class 100 spending throughout the Plan is based on careful management of overtime costs -- something OFM has yet to accomplish. The Department anticipates controlling future overtime costs with initiatives such as FACTS, and the opening of a new centralized maintenance facility.

When the Director of OFM first assembled his staff and assessed the status of City vehicle operations they reached the conclusion that vehicle availability could be increased significantly over the near-term by investing heavily in overtime. As noted in the Plan, this effort produced dramatic increases in availability, although in most cases still below the 80 percent target OFM has established. Whether a vehicle moves through the system quickly is dependent upon circumstances apart from overtime -- parts availability, special requirements and the availability of particular personnel skills -- and efficiency requires a close degree of coordination. Whether OFM can hit its targets will depend upon how its manages the various aspects of its tasks.

Centralized Maintenance Facility -- ***Continued delays in the acquisition of a centralized maintenance facility will effect overtime and the efficiency of OFM***

At the close of FY93 OFM stated that it had narrowed down the selection of a site for a centralized maintenance facility to two prime locations and that site acquisition would be made in early- to mid-FY94. To date no decision has been made as to the final site, current City projections anticipate acquisition in "late FY94 to 1st Quarter FY95" and thus no substantial progress has been made on this vital facility. Whatever the delays surrounding this initiative, they need to be rectified immediately. The City previously has indicated that both controlling overtime and improved parts distribution were dependent on this facility being available, and that the anticipated savings were built into the Plan. PICA Staff will monitor this initiative very closely and report any variance that may develop.

Prison Vehicle Maintenance Facility -- *The Prison System's vehicle maintenance facility also has been delayed*

PICA's 1993 bond issue included $500,000 for the design of a vehicle maintenance facility for the Prisons Department. Design was to be completed in FY94 with construction in FY95. Currently the design stage has been delayed so that the facility can be included in the new House of Correction (HOC) facility (which is currently in the planning stage). Preliminary plans call for the HOC and the Prison System vehicle maintenance facility to be constructed at the same location and to be completed in FY97. OFM is to assist in the design phase and is to be responsible for the ongoing vehicle maintenance at this facility.

MAYOR'S OFFICE OF INFORMATION SERVICES

Primary Areas of PICA Concern

- o Authority of the Chief Information Officer
- o Employee Computer Literacy and Training

Plan Expenditure Projections FY95-FY99 (millions)

	FY95	FY95-FY99
Class 100	$4.8	$24.7
Class 200	4.3	21.9
Class 300/400	.3	1.8
Total	$9.4	$48.4

Introduction

In September 1993 the City of Philadelphia established the Mayor's Office of Information Services (MOIS) under the authority of its Chief Information Officer (CIO) to develop and manage the City's information system policies. In addition, MOIS has assumed the role of the former Philadelphia Computing Center (PCC) which previously provided limited centralized services. The Plan states the mission of MOIS is to provide "the City's centralized and analytical database and software development staff, a computer skills Training Center, an Operational Support Center, a Mainframe Based Data Center, and City-wide Telecommunications Management in support of the City's needs." The Mayor's Office of Information Services has assumed PCC's budget for operational purposes.

The Plan projects that the Office's FY95 obligations will increase $671,092 (7 percent) from FY94. This increase is the result of higher purchase of service (Class 200) costs which includes a new mainframe computer system lease and additional funding for project management support. The Office's Class 100 costs grow 2.5 percent and 2.2 percent in both FY96 and FY97. As is the case with other agencies, these costs show zero growth in FY98 and FY99. The baseline estimate for City-wide information technology products, services, and consulting support in FY94 (taking into account all of the City's operations spread among its various departments) totals $42 million.

In a previous report PICA Staff noted it had met with the CIO and the MOIS Staff and was impressed with their vision and dedication to their task. The Staff Report expressed caution about several areas of the strategic information plan and promised to monitor its progress. The following is an update of some of PICA Staff's previously expressed concerns:

Authority of the Chief Information Officer

Notwithstanding the support of the Mayor expressed in Executive Order No. 11-93 PICA Staff has indicated that it has concerns about the authority of the CIO over operating departments in the area of design and procurement new systems. PICA Staff commented that the lack of firm administrative guidelines could cause implementation delays and inter-departmental fragmentation.

While firm guidelines have yet to be set, and the results of long-term efforts have yet to be seen, the CIO seems to be successfully exercising his oversight authority. In recent PICA Staff meetings with MOIS and other agencies and operating departments there was clear indication of development of a more unified decision making process on computer-related decisions. While authority over the purchase of computer-related equipment has been delegated to the departments for FY95, the CIO has worked with departments to develop a "City First" approach in preparing and administering their budgets. PICA Staff applauds this first step made by the CIO and encourages publication of firmer administrative guidelines that would serve to diminish the potential for bureaucratic battles in the future.

Employee Computer Literacy and Training

PICA Staff has stated that City employees' computer literacy levels must grow with the evolution of the City's MIS system.

As part of MOIS' Strategic Information Technology Plan for 1994-2000 a training and support strategy is being developed to address the growing needs of the City's users. In order to do this, MOIS has sponsored development of a computer learning center at MOIS' 1234 Market Street office. The training center will consist of three fully-equipped classrooms which will offer a curriculum of fully-certified courses. As a part of MOIS' curriculum development the following seven categories of training will be focused upon:

Category	**Example of Class**	**Audience**
Office Automation	All PC Classes	General Users
In-House Applications	Case Management and Records Systems	Specified Users
Planning & Administration	Project Management Communications Skills Cost-Budget Analysis	Specified Users
Re-Engineering Methodology	Group Dynamics Workflow Analysis	Specified Users

Network	LAN Administration	Technical Support Staff
Systems Development	Programming and System Management Training	Programmers
Operations	Mainframe, DOS, MVS and ESA	Programmers and Technical Staffs

Initially MOIS will concentrate on office automation training and schedule introductory and intermediate level PC training classes in the future. Instead of offering large advanced courses, three-hour workshops will be scheduled throughout the year.

Cost Accounting System

In order for the City to judge the productivity of each department and better allocate costs, PICA Staff has observed that significant improvements in the City's cost accounting system are needed, and the City has acknowledged their necessity. Upon implementation, such a tool would help the City allocate costs back to departments, generally improve its knowledge of departmental financial operations and impose greater accountability.

The CIO and the Finance Director have indicated that the updated version of the City's existing Financial and Management Information System (FAMIS) operation should be able to address this need. Phase I of augmented FAMIS is projected to be at full operating capacity by July of 1994 with Phase II (the cost accounting module) coming on line by January of 1996. MOIS has recently held training sessions for Phase I with follow-up sessions to start in May. The CIO has identified the cost accounting module as the system that will give the City the capacity to assess costs and allocate them to departments.

Critical Path Management and Other Project Management Systems

In the past PICA Staff has been critical of the City's not using the critical path method or similar project management programs to avoid many present time-consuming problems and increase the ability of management to gather and use data about its projects. PICA Staff is pleased to see the use of computer based project management by MOIS. The "MOIS project review chart" consolidates team members, project descriptions, effected departments, completion dates and projected costs in a way that can be easily understood. A major benefit of this chart is the use of a schedule that illustrates the key milestones of the project and can illustrate the impact of project delays in the future. PICA Staff is pleased with this development and hopes that it spreads to other departments.

Authority of the Chief Information Officer -- *The lack of firm administrative guidelines jeopardizes the authority of the CIO*

As stated above, PICA Staff commends the CIO on the progress he has made to date in improving the City's information systems. He has united operating departments under his leadership with "City First" groups. The Mayor has given the CIO support through Executive Order No. 11-93, by giving him approval authority on all purchases related to information services (although implementation and preservation of that authority will be an ongoing challenge). PICA Staff has stated earlier (and reiterates) the need for firmer expenditure control authority for the CIO. An ideal example would be the authority of the Fleet Manager, who has consolidated the City-wide vehicle budget within his agency and under his control. One of the major reasons for the failure of PCC was its inability to control purchasing or management decisions individual departments made regarding information services.

Employee Computer Literacy and Training -- *Training City employees will be a challenge for MOIS*

In a recent meeting the CIO indicated that approximately 6,000 City employees need some type of computer training. While the establishment of a computer learning center is key, getting employees trained may be more difficult. Based on information provided to PICA, the power of MOIS to mandate that City employees take classes is not yet clear. Currently, MOIS is making employees more aware of training needs through advertisements and videos. While this may be effective for some, it may fail to motivate the most reluctant. As noted above, the impact of technological change is not the same for everyone, and any training program must recognize that, but the City's work force has little option but to become computer literate.

OTHER SIGNIFICANT PLAN CONCERNS

Primary Areas of PICA Concern

- o Commerce -- Economic Stimulus Program
- o Extraordinary Contracts and Cooperation Agreement Reporting -- City Compliance
- o First Judicial District -- Fee Collections
- o Management and Productivity -- Strategic Plan
- o PGW -- Status of Litigation
- o Recreation -- Camp William Penn Closure Decision
- o Recreation/Fairmount Park Commission -- Consolidation of Duplicative Services

Commerce -- *PICA Staff has not evaluated the Philadelphia Economic Stimulus Program as part of its Plan review*

In response to on-going job losses, the City is developing a Philadelphia Economic Stimulus Program which is projected to utilize $2.2 billion in public and private funding to revitalize the City's economy over a three-year period. The Stimulus Program is still in the planning stages and PICA does not anticipate undertaking a detailed review until its approval by City Council. PICA Staff is satisfied that the projected results in the Plan do not depend upon either the approval of the Stimulus Program or its successful implementation, and offers no opinion on it at this time.

Extraordinary Contracts and Cooperation Agreement Reporting -- *PICA continues to receive Extraordinary Contracts that are not in compliance with Cooperation Agreement requirements, and the City has been delinquent in filing some Cooperation Agreement mandated reports*

The Cooperation Agreement requires that the City submit a certification as to Plan compliance from the Director of Finance to PICA for all contracts valued at more than $1 million in a single year or $5 million over the life of the Plan. This provision was built into the Cooperation Agreement to provide both the City and PICA with an early warning mechanism when contracts were costing more than the Plan anticipated.

As of the end of the third quarter of FY94 PICA Staff continues to receive Extraordinary Contracts that are late, inaccurate, improperly submitted or out of compliance. On one occasion the City submitted a prison health care contract as being in compliance with the Plan when little more than cursory review showed it to be $3 million over budgeted costs. PICA Staff continues to address this matter with the City, in the hope that it will begin to utilize this tool as an early indication as to departmental budget compliance as well as to comply with the Cooperation Agreement.

The Cooperation Agreement anticipates the Authority's receipt of several reports on an ongoing basis (see Appendix A). While Quarterly Reports have been received as scheduled, the City, particularly in recent months, has failed to provide others.

First Judicial District (FJD) Fees Collection -- *Fee receipts remain below estimates*

As discussed in the Police Department section of this report, Traffic Court fees continue to come in well below original estimates. The Monthly Managers' Report (for the month ending January 31, 1994) projects Traffic Court revenues to be $3 million for FY94 ($5 million less than originally projected). In meetings with PICA Staff, FJD staff has indicated that the problem involves both a decrease in traffic violation citations issued and lack of stringent enforcement. FJD has indicated that a more stringent statue of limitations policy and increased "boot" enforcement may help to correct this problem. Traffic collections over the life of the Plan have been projected to be $3.6 million. FJD Staff indicated they will continue to focus on enforcement in order to attempt to meet or surpass this projected amount, although PICA Staff is concerned that poor financial performance may be indicative of more serious legal and systemic problems. The results of a recently announced collection program may be informative in that regard.

Management and Productivity -- *Development of the City's Strategic Plan continues*

In prior reports PICA Staff has offered its thoughts on the need for, and suggested the emphasis of, a City strategic plan. The Rendell Administration has convened a task force that is currently working on such a strategic plan, and PICA Staff is impressed by its commitment. PICA Staff expects to review the Strategic Plan once it is formalized.

PGW -- *There is current litigation challenging the $18 million "offset" that PGW gives to the City annually*

Currently, the City receives an $18 million annual rental offset from PGW, and there is litigation challenging the legality of the City to do so. General Fund loss of this revenue item would have a negative $90 million impact on the Plan and require the City to either cut back appropriations in other areas or seek additional revenue from other sources. Commonwealth Court recently ordered PGW to not make a $4.5 million transfer to the City representing the final payment for FY94, which in turn raises questions about the payment in FY95 and the out-years of the Plan which could aggregate $94.5 million under the worst case alternative. PICA Staff will monitor the progress of the litigation.

Recreation Department -- ***No final decision has been made on the future of Camp William Penn***

Scarcity of funds and fewer encampment days have caused the City to contemplate the closing or privatization of Camp William Penn. In a recent meeting with PICA Staff, the Recreation Commissioner indicated that further funding reductions could make the camp's operation unmanageable. As in other areas, the City has both the right and obligation to make policy decisions concerning Camp William Penn. If it determines that City support of an overnight camping program should continue, the City should assess options ranging from soliciting outside support for the current facility to the sale of the Camp and re-allocation of resources to procuring camp nights at other facilities.

Recreation Department and Fairmount Park Commission -- ***The Recreation Department and the Fairmount Park Commission continue to provide duplicate services for some parts of the City, and maintain largely separate maintenance operations***

As a cost saving initiative, since the initial Plan the City has alluded to efforts to consolidate some of the duplicative services provided by the Recreation Department and the Fairmount Park Commission. Both entities have expressed a general willingness to work together but not a particular willingness to compromise. The creation of a central facilities maintenance agency could address operations and maintenance concerns, but PICA Staff encourages the Managing Director to place a high priority on addressing programmatic problems.

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APPENDIX A

Statutory Background and Chronology

Overview

The General Assembly created PICA in June of 1991 by its approval of The Pennsylvania Intergovernmental Cooperation Authority Act for Cities of the First Class (Act of June 5, 1991, P.L. 9, No. 6), and critical events have occurred since that action which are of value to in assessing the efforts of both the Authority and the City to meet their respective responsibilities. As in previous PICA Staff reports concerning the City's prior five-year financial plans, rather than re-state in the body of this Staff Report the principal provisions of the PICA Act, the Intergovernmental Cooperation Agreement and the Authority's history, PICA Staff has included such information in this Appendix.

Statutory Basis -- The PICA Act

The mission of the Authority, as stated in the PICA Act (Section 102), is as follows:

> Policy.--It is hereby declared to be a public policy of the Commonwealth to exercise its retained sovereign powers with regard to taxation, debt issuance and matters of Statewide concern in a manner calculated to foster the fiscal integrity of cities of the first class to assure that these cities provide for the health, safety and welfare of their citizens; pay principal and interest owed on their debt obligations when due; meet financial obligations to their employees, vendors and suppliers; and provide for proper financial planning procedures and budgeting practices. The inability of a city of the first class to provide essential services to its citizens as a result of a fiscal emergency is hereby determined to affect adversely the health, safety and welfare not only of the citizens of that municipality but also of other citizens in this Commonwealth.
>
> Legislative intent.--
>
> (1) It is the intent of the General Assembly to:
>
> (i) provide cities of the first class with the legal tools with which such cities can eliminate budget deficits that render them unable to perform essential municipal services;
>
> (ii) create an authority that will enable cities of the first class to access capital markets for deficit elimination and seasonal borrowings to

avoid default on existing obligations and chronic cash shortages that will disrupt the delivery of municipal services;

(iii) foster sound financial planning and budgetary practices that will address the underlying problems which result in such deficits for cities of the first class, which city shall be charged with the responsibility to exercise efficient and accountable fiscal practices, such as:

(A) increased managerial accountability;

(B) consolidation or elimination of inefficient city programs;

(C) recertification of tax-exempt properties;

(D) increased collection of existing tax revenues;

(E) privatization of appropriate city services;

(F) sale of city assets as appropriate;

(G) improvement of procurement practices including competitive bidding procedures;

(H) review of compensation and benefits of city employees; and

(iv) exercise its powers consistent with the rights of citizens to home rule and self government.

(2) The General Assembly further declares that this legislation is intended to remedy the fiscal emergency confronting cities of the first class through the implementation of sovereign powers of the Commonwealth with respect to taxation, indebtedness and matters of Statewide concern. To safeguard the rights of the citizens to the electoral process and home rule, the General Assembly intends to exercise its power in an appropriate manner with the elected officers of cities of the first class.

(3) The General Assembly further declares that this legislation is intended to authorize the imposition of a tax or taxes to provide a source of funding for an intergovernmental cooperation authority to enable it to assist cities of the first class and to incur debt of such authority for such purposes; however, the General Assembly intends that such debt shall not be a debt or liability of the Commonwealth or a city of the first class nor shall debt of the authority payable from and secured by such source of funding create a charge directly or indirectly against revenues of the Commonwealth or city of the first class.

The PICA Act establishes requirements for the content of a five year financial plan, and Sections 209 (b)-(d) of the statute and the Cooperation Agreement provide:

(b) Elements of plan. -- The financial plan shall include:

(1) Projected revenues and expenditures of the principal operating fund or funds of the city for five fiscal years consisting of the current fiscal year and the next four fiscal years.

(2) Plan components that will:

(i) eliminate any projected deficit for the current fiscal year and for subsequent years;

(ii) restore to special fund accounts money from those accounts used for purposes other than those specifically authorized;

(iii) balance the current fiscal year budget and subsequent budgets in the financial plan through sound budgetary practices, including, but not limited to, reductions in expenditures, improvements in productivity, increases in revenues, or a combination of these steps;

(iv) provide procedures to avoid a fiscal emergency condition in the future; and

(v) enhance the ability of the city to regain access to the short-term and long-term credit markets.

(c) Standards for formulation of plan:

(1) All projections of revenues and expenditures in a financial plan shall be based on reasonable and appropriate assumptions and methods of estimation, all such assumptions and methods to be consistently applied.

(2) All revenue and appropriation estimates shall be on a modified accrual basis in accordance with generally accepted standards. Revenue estimates shall recognize revenues in the accounting period in which they become both measurable and Available. Estimates of city-generated revenues shall be based on current or proposed tax rates, historical collection patterns, and generally recognized econometric models. Estimates of revenues to be received from the state government shall be based on historical patterns, currently available levels, or on levels proposed in a budget by the governor. Estimates of revenues to be received from the federal government shall be based on historical patterns, currently available levels, or on levels proposed in a budget by the president or in a congressional budget resolution. Non-tax revenues shall be based on current or proposed rates, charges or fees, historical patterns and generally recognized econometric models. Appropriation estimates shall include, at a minimum, all obligations incurred during the fiscal years and estimated to be payable during the fiscal year or in the 24-month period following the close of the current fiscal year, and all obligations of prior fiscal years not covered by encumbered funds from prior fiscal years. Any deviations from these standards of estimating revenues and appropriations proposed to be used by a city shall be specifically disclosed and shall be approved by a qualified majority of the board.

(3) All cash flow projections shall be based upon reasonable and appropriate assumptions as to sources and uses of cash, including, but not limited to, reasonable and appropriate assumptions as to the timing of receipt and expenditure thereof and shall provide for operations of the assisted city to be conducted within the resources so projected. All estimates shall take due account of the past and anticipated collection, expenditure and service demand experience of the assisted city and of current and projected economic conditions.

(d) Form of plan. -- Each financial plan shall, consistent with the requirements of an assisted city's home rule charter or optional plan of government:

(1) be in such form and shall contain:

(i) for each of the first two fiscal years covered by the financial plan such information as shall reflect an assisted city's total expenditures by fund and by lump sum amount for each board, commission, department or office of an assisted city; and

(ii) for the remaining three fiscal years of the financial plan such information as shall reflect an assisted city's total expenditures by fund and by lump sum amount for major object classification;

(2) include projections of all revenues and expenditures for five fiscal years, including, but not limited to, projected capital expenditures and short-term and long-term debt incurrence and cash flow forecasts by fund for the first year of the financial plan;

(3) include a schedule of projected capital commitments of the assisted city and proposed sources of funding for such commitments; and

(4) be accompanied by a statement describing, in reasonable detail, the significant assumptions and methods of estimation used in arriving at the projections contained in such plan.

The Cooperation Agreement (at Section 4.04(a)-(h)), and similar provisions of the PICA Act, also require the following as supporting data for the Plan:

(a) a schedule of debt service payments due or projected to become due in respect of all indebtedness of the City and all indebtedness of others supported in any manner by the City (by guaranty, lease, service agreement, or otherwise) during each fiscal year of the City until the final scheduled maturity of such indebtedness, such schedule to set forth such debt service payments separately according to the general categories of direct general obligation debt, direct revenue debt, lease obligations, service agreement obligations and guaranty obligations.

(b) a schedule of payments for legally mandated services included in the Financial Plan and due or projected to be due during the fiscal years of the City covered by the Financial Plan;

(c) a statement describing, in reasonable detail, the significant assumptions and methods of estimation used in arriving at the projections contained in the Financial Plan;

(d) the Mayor's proposed operating budget and capital budget for each of the Covered Funds for the next (or in the case of the initial Financial Plan, the current) fiscal year of the City, which budgets shall be consistent with the first year of the Financial Plan and which budgets shall be prepared in accordance with the Home Rule Charter;

(e) a statement by the Mayor that the budgets described in section 4.04(d) hereof:

(i) are consistent with the Financial Plan;

(ii) contain funding adequate for debt service payments, legally mandated services and lease payments securing bonds of other government agencies or of any other entities; and

(iii) are based on reasonable and appropriate assumptions and methods of estimation.

(f) a cash flow forecast for the City's consolidated cash account for the first fiscal year of the City covered by the Financial Plan;

(g) an opinion or certification of the City Controller, prepared in accordance with generally accepted auditing standards, with respect to the reasonableness of the assumptions and estimates in the Financial Plan; and

(h) a schedule setting forth the number of authorized employee positions (filled and unfilled) for the first year covered by such Financial Plan for each board, commission, department or office of the City, and an estimate of this information for the later years covered by the Financial Plan. The schedule required under this paragraph (h) shall be accompanied by a report setting forth the City's estimates of wage and benefit levels for various groups of employees, such information to be presented in a manner which will allow the Authority to understand and effectively review the portions of the Financial Plan which reflect the results of the City's labor agreements with its employees, and an analysis of the financial effect on the City and its employees of changes in compensation and benefits, in collective bargaining agreements, and in other terms and conditions of employment, which changes may be appropriate in light of the City's current and forecast financial condition. The parties agree to cooperate such that the form of the report required under this paragraph (h), and the subjects covered, are reasonably satisfactory to the Authority.

City Reporting and Variances

The PICA Act (Section 209) and the Cooperation Agreement (Section 409(b)) require submission of quarterly reports by the City on its compliance with the Plan within 45 days of the end of a fiscal quarter. If a quarterly report indicates that the City is unable to project a balanced Plan and budget for its current fiscal year, the Authority may by the vote of four of its five appointed members declare the occurrence of a "variance", which is defined in Section 4.10 of the Cooperation Agreement as follows:

> (i) a net adverse change in the fund balance of a Covered Fund of more than one percent (1%) of the revenues budgeted for such Covered Fund for that fiscal year is reasonably projected to occur, such projection to be calculated from the beginning of the fiscal year for the entire fiscal year, or (ii) the actual net cash flows of the City for a Covered Fund are reasonably projected to be less than ninety-five percent (95%) of the net cash flows of the City for such Covered Fund for that fiscal year originally forecast at the time of adoption of the budget, such projection to be calculated from the beginning of the fiscal year for the entire fiscal year.

As defined in Section 1.01 of the Cooperation Agreement, the City's "Covered Funds" are the General Fund, General Capital Fund, Grants Revenue Fund and any other principal operating funds of the City which become part of the City's Consolidated Cash Account.

The statute mandates the submission of monthly reports to PICA by the City after determination by the Authority of the occurrence of a variance.

As provided in Section 210(e) of the PICA Act, there are legal consequences flowing from a determination by the Authority that a variance exists, and in addition to the City's additional reporting responsibilities, it also is required develop revisions to the Plan necessary to cure the variance. The remedies which PICA has available to it to deal with a continuing uncorrected variance are to direct the withholding of both specific Commonwealth funds due the City, and that portion of the 1.50% tax levied on the wages and income of residents of the City in excess of the amounts necessary to pay debt service on PICA's bonds. Any amounts withheld would be paid over to the City after correction of the variance.

Major PICA Events

PICA's creation was an action taken by the Commonwealth in direct reaction to Philadelphia's fiscal crisis, and its work during its first year of existence was to assist the City to avoid insolvency and in its efforts to lay the foundation for its return to fiscal stability. The negotiation of the Cooperation Agreement to set out the basic terms of the City-PICA relationship, review of an initial five-year financial plan and the issuance of bonds to provide funding to permit the City to stabilize its budget and cash needs were the most critical tasks at hand. Since the issuance by PICA of the first series of its bonds in June of 1992, following successfully defended challenges to the constitutionality of the PICA Act, PICA has devoted its primary attention to the assessment of Plan progress, additional borrowing for City capital projects, evaluation of City reporting, analysis of City practices and programs and oversight of the capital projects for which PICA has borrowed almost $294 million for use by the City. The following notes in summary form the major events since the Authority's creation:

June 5, 1991	PICA Act approved by Governor Robert P. Casey.
June 25, 1991	Initial organizational meeting of the Authority.
January 3, 1992	Approval by City Council and Mayor W. Wilson Goode of the Cooperation Agreement ordinance.
January 8, 1992	Execution of the Cooperation Agreement by PICA and Mayor Edward G. Rendell.
February 20, 1992	Submission by Mayor Rendell of proposed initial Plan for FY92-FY96 to City Council.
	Public employee labor unions file legal action with the Pennsylvania Supreme Court alleging unconstitutionality of PICA Act.
March 5, 1992	Approval of initial Plan by City Council and submission to PICA.

April 6, 1992	PICA approval of initial Plan.
April 13, 1992	Supreme Court declares the PICA Act to be constitutional.
April 21, 1992	Submission to PICA by Mayor Rendell of amendments to the initial Plan.
April 27, 1992	Public employee labor unions file for reconsideration of Supreme Court decision.
May 18, 1992	Submission to PICA by Mayor Rendell of further amendments to the Plan.
	PICA approval of amended Plan.
May 29, 1992	Supreme Court issues written opinion supporting the constitutionality of the PICA Act, and denying unions' request for reconsideration.
June 16, 1992	PICA issues $474,555,000 in Special Tax Revenue Bonds (City of Philadelphia Funding Program), Series of 1992.
August 16, 1992	PICA receives first City quarterly Plan report (for the fourth quarter of FY92).
October 15, 1992	City completes negotiation of labor agreements with District Councils 33 and 47 of the American Federation of State, County and Municipal Employees.
October 19, 1992	PICA authorizes initial transfer of Authority bond proceeds for capital projects ($21.7 million).
November 16, 1992	PICA receives City quarterly Plan report for first quarter of FY93, projecting a variance in the Plan through June 30, 1993 of $57 million (2.5 percent) of budgeted revenues of the General Fund.
December 9, 1992	PICA Board declares existence of "variance" in Plan, requiring monthly City reporting.
January 21, 1993	Mayor Rendell proposes FY93 variance correction measures, FY94-FY98 revised five-year financial plan and FY94 capital budget to Philadelphia City Council.

March 18, 1993	City Council completes action on FY93 variance correction measures, FY94-FY98 revised five-year financial plan and FY94 capital budget.
March 19, 1993	Mayor Rendell submits the City's "Five-Year Financial Plan, Fiscal Year 1994 - Fiscal Year 1998 (including Fiscal Year 1993)" to Authority in compliance with PICA Act requirement for annual Plan revision, and to propose measures to correct variance declared by PICA on December 9, 1992.
March 31, 1993	Act 111 Police arbitration panel issues its award concerning the City and F.O.P. Lodge No. 5.
April 13, 1993	The F.O.P. Lodge No. 5 files an appeal of the Act 111 arbitration award, and the City files a cross-appeal. PICA is not named as a party to the litigation. On May 20, 1993, the Court of Common Pleas for Philadelphia County upholds the award, finding for the City on the major economic issues. Both the City and the F.O.P. Lodge No. 5 file appeals to the Commonwealth Court of Pennsylvania which, on December 7, 1993, rules in favor of the City on all issues raised by the City and the F.O.P. Lodge No. 5. On January 6, 1994, the F.O.P. Lodge No. 5 files a petition for allowance of appeal to the Pennsylvania Supreme Court, which is denied on April 28, 1994.
April 14, 1993	PICA Board approves the FY94-FY98 Plan, and the measures proposed by the City to remedy the Variance. As part of its approval of the FY94-FY98 Plan, the Authority also approves in principle the use of $23.5 million in remaining proceeds of the Authority's Series of 1992 bond issue not required to be used to fund the City's FY92 deficit to fund a special indemnity account directed towards reducing the City's outstanding indemnity exposure.
July 12, 1993	PICA Board approves a list of capital projects as being eligible for PICA financing.
July 23, 1993	PICA issues $643,430,000 in aggregate principal amount of its "Special Tax Revenue Bonds (City of Philadelphia Funding Program), Series of 1993". The bond issue

	funds $195 million in capital projects and also refunds $381 million in City general obligation debt.
August 19, 1993	PICA issues $178,675,000 in aggregate principal amount of its "Special Tax Revenue Refunding Bonds (City of Philadelphia Funding Program), Series of 1993A". The bond issue refunds $150 million of the Authority's Series of 1992 bonds.
November 21, 1993	Act 111 fire arbitration panel issues its award concerning the City and I.A.F.F. Local 22.
December 21, 1993	I.A.F.F. Local 22 files an appeal from the Act 111 arbitration award, and the City files a cross-appeal. PICA is not named as a party to the litigation. The Court of Common Pleas for Philadelphia County has not yet rendered its decision.
January 13, 1994	Mayor submits to City Council the City's proposed "Five-Year Financial Plan, Fiscal Year 1995 - Fiscal Year 1999 (including Fiscal Year 1994)", the City's proposed General Fund budget for the 1995 Fiscal Year and the 1995 Fiscal Year capital budget.
March 24, 1994	City Council approves the FY95-FY99 Plan and the City's General Fund and capital budgets for FY95.
April 4, 1994	Mayor submits the FY95-FY99 Plan to PICA.

Future City Reporting to PICA

As discussed in the section of this Report entitled "Executive Summary and Staff Recommendation", absent the occurrence of a variance, receipt of an arbitration award which is at variance with the Plan or a determination by the City that further revisions to the Plan are necessary, the City will not submit a revised Plan to the Authority until March of 1995. During future months, the Authority will receive quarterly reports on the City's performance under the Plan, together with other data.

The reporting system established in the Cooperation Agreement and the PICA Act anticipates a regular flow of data to PICA, and the reporting system which has been established by agreement between the City and PICA under the provisions of the PICA Act is divided into several groups, which are described below:

Quarterly Plan Reports. The Authority receives reports from the City on a quarterly basis (45 days after the end of each fiscal quarter) concerning the status of compliance with the Plan and associated achievement of initiatives. The remaining quarterly reporting deadlines for FY94 are May 16, 1994 and August 15, 1994. Quarterly reporting deadlines for FY95 are November 14, 1994, February 14, 1995, May 15, 1995 and August 15, 1995. The Cooperation Agreement also requires that the City provide reports to PICA concerning Supplemental Funds (*i.e.*, the Water and Aviation Funds) on a quarterly basis.

Grants Revenue Fund Contingency Account Report. The Cooperation Agreement provides that a report on the Grants Revenue Fund Contingency Account be prepared and submitted, by department, not later than 20 days after the close of each fiscal quarter, and those yet to be received relating to FY94 are: April 20, 1994 (which has not yet been received) and July 20, 1994. For FY95 the reporting dates are October 20, 1994, January 20, 1995, April 20, 1995 and July 20, 1995. This report details the receipt and use of Federal and Commonwealth Funds by the City, as well as the eligibility for fund withholding by the Commonwealth at PICA's direction in the event the City cannot balance the Plan after a variance has been declared, and followed by an extended period of intensive reporting and PICA review of proposed corrective efforts.

Prospective Debt Service Requirements Reports. The Cooperation Agreement requires submission of a report detailing prospective debt service payments by the City, as well as lease payments, 60 days prior to the beginning of a fiscal quarter. The remaining report in this category for FY94 is to be received on May 2, 1994. The dates for submission of such reports for FY95 are August 1, 1994, November 1, 1994, January 3, 1995 and May 1, 1995.

PERSONAL VIEWS OF PICA BOARD MEMBERS

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PERSONAL VIEWS OF HILIARY H. HOLLOWAY

As a new member of the PICA Board, but as one who has long been involved with City government from different perspectives, I participated in several of the review sessions between PICA Staff and representatives of City departments. I was impressed by the level of detail of the discussions, and the sense of collaborative effort directed towards a common goal, which occurred in most of the meetings.

I came away from the reviews, and my examination of the FY95-FY99 Plan, with the impression that the City has made large strides in its efforts, but that much still remains to be done. Senior departmental staff for the most part show both detailed knowledge of, and commitment to, the tasks of their agencies, but a sense of overall direction and coordination under the guidance of a commonly agreed-upon set of strategic goals and principles (beyond the production of a balanced budget) seems to be lacking. The City's strategic plan, when adopted, should provide a sense of common direction and larger policy context in which officials can act, and I echo the prior statements of my PICA colleagues in support of the process.

Integral to the success of the Rendell Administration's work to administer the City's business in a more efficient manner will be the successful completion of initiatives to assert greater control and direction over critical central services. Changes to the City's financial accounting and management information system to provide the capacity to manage with better data and allocate expenses to those who incur them are now being made, but should have had a higher priority in the first year of the Administration -- even recognizing that the pressures of the fiscal crisis understandably distracted senior policy makers from addressing longer-term structural problems in the detail they deserved. Broad-based reorganization of the fleet management, information systems and risk management functions, and the prospect for major changes in the manner in which the City maintains its facilities, provide the potential for great benefits. Experience, however, has taught me that those benefits will be realized only when most of the organization is moving in the same direction. The management of change is more difficult than creation of the structure for it.

Philadelphia's achievement of a balanced budget is a milestone along the road back to fiscal stability, and only a foundation for the larger and more difficult task of re-making City government, restoring the tax base and improving services to business and individuals. The loss of population and employment over the past twenty years is a tragedy. It has been manifested in the decline of once-vibrant neighborhoods and the disappearance of the thousands of the jobs which historically have been the basis for stable families, good schools, safe communities and predictable city revenues.

PICA's statutory goal is to assist the City to regain solvency, restoration of investment grade ratings and access to the national credit markets, and I am optimistic that we will reach that goal during 1994. This Authority has provided financial tools, oversight and commentary, but the long-run success of Philadelphia will depend -- as it always has -- on the willingness of its elected and appointed officials, as well as citizens who are not involved in government on a daily basis, to put aside their differences in the hopes of making our city a better place.

I am pleased to have been given an opportunity to play a part.