# Pennsylvania Intergovernmental Cooperation Authority

**Staff Report**
**on the**
**City of Philadelphia's**
**Five-Year Financial Plan**
**for**
**Fiscal Year 1996 - Fiscal Year 2000**

**April 17, 1995**

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## TABLE OF CONTENTS

## INTRODUCTION AND STAFF RECOMMENDATION

The City of Philadelphia's Five-Year Financial Plan, Fiscal Year 1996-Fiscal Year 2000 (including Fiscal Year 1995), submitted to the Pennsylvania Intergovernmental Cooperation Authority (PICA) as of March 16, 1995 (the "FY96-FY2000 Plan" or the "Plan") presents a reasonable prospect for balanced budgets in each year of its term. As in prior years, this year's Plan is dependent on a variety of circumstances, many of which are beyond the City's control. The results of collective bargaining and arbitration processes that will determine new labor contracts effective in FY97 and later years, the final four years of the Plan, will be critical to the overall success of the Plan. The Plan also relies on the realization of a highly speculative revenue source, tax revenues from riverboat gambling. As a result, while the Plan's projections are reasonable, there is a high degree of uncertainty involved in its most basic assumptions.

*Tax Cut Proposal*

A major element of the FY96-FY2000 Plan is its proposal to reduce and restructure two of the City's major tax revenue sources, the Wage, Earnings and Net Profits taxes and the Business Privilege Tax. In the opinion of PICA Staff, the Plan's proposed tax cut is neither so small as to be insignificant to the typical taxpayer, nor so large as to be unrealistic given the financial constraints likely to exist over the FY96-FY2000. Nonetheless, it is important to recognize that year-by-year determinations will have to be made about the feasibility of implementation of additional incremental tax reductions as currently proposed.

Projecting a tax cut in the FY96-FY2000 Plan in some respects is easy given the fairly optimistic assumptions that the Plan makes with respect to revenues from riverboat gambling and the impact of future labor contracts. If either of those assumptions are not realized, or if other adverse events occur such as a reduction in revenue growth due to a national recession, implementing the tax cuts projected in the Plan may be quite difficult. Substantial additional revenues or savings from new management and productivity initiatives may have to be achieved to generate the resources for the tax cuts.

*Strategic Planning*

PICA Staff believes that the completion of the strategic planning process and implementation of the Strategic Plan is critical to the City's continuing success beyond FY2000. The Citywide Strategic Plan document that is included as an appendix to the FY96-FY2000 Plan is the outcome of Phase I of the City's strategic planning process. This document provides a framework for Phase II of the process, under which each department and key interagency group will produce a plan that will implement the Citywide plan. Producing a clear and comprehensive statement of the City's goals and general approaches to achieving them is an important accomplishment. But it is essential that departmental planning as part of Phase II take place, and that these plans are implemented, if the City's goals are to be achieved.

*Plan Structure*

The FY96-FY2000 Plan is the fourth in a series of Five-Year Financial Plans that have been submitted annually to PICA since 1992. This year's Plan, like last year's, is significantly different from the first two Plans in its basic structure. The first two Plans included baseline obligation projections for each department and projections of the financial impact of initiatives to increase revenues and reduce expenditures. The impact of these initiatives was reduced by a certain percentage to account for potential failure of implementation and then incorporated into departmental projections.

In the last year's and this year's Plans, initiatives have been described, and the results have been estimated for past and current years, and projected for only one year. The impact of the initiatives has not been incorporated directly into Plan projections. In some cases, Plan projections have been based on explicit assumptions about the impact of management actions, but these assumptions are sometimes not included in the Plan document, although they have been provided to PICA Staff. As a result in the change in methodology, Plan projections have come to rely more heavily on the reasonableness of the baseline projection growth rates.

The change in the structure of the Plan over the past four years is also reflected in the narrative of the Plan documents, which has evolved from a discussion of a planned course of action and its financial effects, to a description of past accomplishments and future issues that have to be addressed, without specifically indicating how they will be addressed. In short, the Plan has evolved from a presentation focusing on baseline financial projections and supporting quantified initiatives to increase revenues and reduce costs, which clearly delineates the Administration's contemplated course of action and its financial impacts, to a more generalized forecast document which essentially indicates maintenance of current personnel and service levels and is driven largely by base obligation growth assumptions.

The trend described above to some degree reflects the improved financial condition of the City. It also reflects that fact that the final four years of the FY96-FY2000 Plan are to a large extent undiscovered country due to the expiration of the current labor contracts on June 30, 1996. The Plan projects no Class 100 (salary) cost increases aside from that which will occur under current labor contracts. The Plan implicitly assumes that any additional wage increases under labor contracts beginning in FY97 will be paid for through reductions in benefit costs, measures to reduce the rate of increase in benefit costs from Plan-projected levels, or other management and productivity initiative savings. Thus, the change in the Plan's structure can be explained by the difficulty of projecting wage increases that may be required under future contracts and savings from initiatives that may be required to maintain Plan balance as a result. At the same time, the fact that the City is now in a position of being able to balance its budget for the current and next fiscal years without substantial new initiatives also enables a Plan document with few specifics about future changes.

*City Controller's Findings*

In accordance with Section 4.04 (g) of the Intergovernmental Cooperation Agreement between PICA and the City, the City Controller's Office submitted to PICA its opinion with respect to the reasonableness of the assumptions and estimates in the Plan. PICA Staff is grateful for the assistance provided by the Controller's staff in evaluating this Plan. Listed below are some of the major findings of the Controller's Office resulting from its review of the Plan that are not addressed in other sections of this Staff Report:

- The Plan assumes that if Federal funding for Department of Public Health and Homeless programs is reduced, then program spending will be scaled down accordingly, and there will be no impact on the General Fund.

- It is not certain that estimates in the Plan of approximately $3 million per year of revenue from payments in lieu of taxes from nonprofit organizations will be realized.

- The Plan does not include any estimate for back rents and royalties owed by the Phillies, which the Controller's Office estimates are almost $5 million.

- The Plan projection of City pension payment obligations is based on an actuarial assumption of a rate of return on investments of 9 percent, which is an optimistic assumption when compared to other public pension funds. The Controller's Office calculates that for every 0.5 percent decline in the rate of return, there will be a corresponding shortfall in pension fund earnings of approximately $10 million.

- The State legislature is considering legislation that would mandate that the City pay all uniformed personnel 100 percent of pre-injury salary when those employees are injured on duty, and allow the injured person to receive treatment by their own physician after 30 days. The cost of this legislation has been estimated at $2.4 million annually, but this cost is not reflected in the Plan.

- The courts have operated since FY92 under a "zero-growth" budget agreement that has recently been extended through FY97. The Plan does not account for changes in the court budget that would occur under the agreement as a result of savings of approximately $4.6 million due to lease consolidations that will follow the opening of the new Criminal Justice Center. Also, the revenue and obligation projections in the Plan do not reflect potential increases in court revenue, one-third of which would be allocated to an increase in the court budget under the zero-growth agreement.

- The FY96 Governor's budget, according to State officials, contains appropriations to pay approximately 50 percent of Statewide costs of County prisoners in State mental health institutions, while the Plan assumes full State funding of these costs, consistent with the practice since FY93. The potential risk to the Plan is between $1 million and $2 million annually.

- Because of the management and fiscal difficulties at the Philadelphia Gas Works (PGW), there is still some uncertainty that planned cost cutting and revenue enhancement will be fully implemented and sufficient to meet PGW's debt service coverage requirements in FY95. This could adversely affect PGW's ability to make its $18 million annual payment to the General Fund.

- There is a slight risk in the FY98-FY2000 period that cost pressures or a change in revenue patterns could necessitate the Water Fund to forego its annual "scoop" payment to the General Fund.

- The FY96 Governor's budget eliminated "Sewage Treatment Plant Operations Grants". Unless this funding is restored by the State legislature, the Water Fund will suffer an annual shortfall of approximately $6 million.

**Staff Recommendation**

PICA Staff recommends that the Pennsylvania Intergovernmental Cooperation Authority approve the Plan as submitted to the Authority on March 16, 1995.

# EXECUTIVE SUMMARY

## Capital Program Office

PICA Staff's most fundamental concern with respect to the capital program is that the City continues to prepare capital budgets without the guidance of a strategic plan. The critical issue that needs to be addressed through the strategic plan process is what configuration of facilities the City should have to deliver desired services efficiently and effectively. This issue has not been addressed in the development of the Citywide Strategic Plan, but should be addressed in departmental strategic plans. PICA Staff's other concerns relating to the City's capital program are inadequate information to monitor projects, and continued lack of reliance on organized project management techniques to manage projects. While preventive maintenance funding has increased, PICA Staff believes the funding still falls short of what is needed.

## Strategic Plan

The completion of a Citywide Strategic Plan is a major step forward. However, the process must continue through development of departmental strategic plans within the framework of the Citywide Plan. Some of PICA Staff's concerns relating to the Strategic Plan and its relationship to the FY96-FY2000 Plan are described below.

The Plan notes the need to evaluate opportunities to divest from select services, such as providing subsidies to cultural institutions, county functions, services that are inappropriate to departmental missions, and functions that may be more effectively provided through private sector or public authorities, such as the functions of the Philadelphia International Airport, Water Department, and Philadelphia Gas Works. Selective divestment of functions is an issue that PICA Staff believes should receive a high level of emphasis in development of departmental strategic plans.

The Strategic Plan includes elements relating to public education. PICA Staff is concerned about the need for additional funding to implement the strategies to expand school readiness and improve support to families through Family Centers, Youth Access Centers and Community Schools. The long-term needs of the school system in general for support from the City tax base is also a concern.

Strategic planning for services to low-income persons and families is a major need cited in the Citywide Strategic Plan. This should be addressed through departmental and interagency group planning.

PICA Staff is concerned about the availability of funding to expand positive alternatives to crime and drugs, and to institute a more effective incarceration policy that would end the prison cap, bring on line new facilities, and expand use of alternatives to incarceration. Other key strategic issues are greater intergovernmental cooperation with the State government with respect to funding of county functions and regional cooperation.

**Economic Stimulus Program**

The Economic Stimulus Program (ESP) is a major effort to improve the City's economic performance by taking a coordinated and proactive approach to economic development. PICA Staff's primary concern with respect to the ESP is that the Plan does not discuss the issue of program evaluation and how resources are allocated to produce the greatest economic impact.

The Plan's proposal to reduce the Wage, Earnings and Net Profits taxes, and reduce and restructure the Business Privilege Tax would significantly reduce the disparity in tax burden between Philadelphia and competitor locations, which would address one of the most significant impediments to economic development in the City. While further progress will still be needed in tax reduction and restructuring, the Plan proposal, if implemented, would be a very important step in the right direction.

**Current Status of the FY92-FY96 Plan's Management Initiatives**

PICA Staff reviewed the original FY92-FY96 Plan to determine the extent to which the initiatives it projected were implemented, and the issues it raised have been addressed.

With respect to structural changes, much has been achieved, but much remains to be done. Personnel reforms so that hiring, promotion and compensation under the civil service system will promote performance goals, have not been achieved. Substantial changes to the Charter have not been enacted, due to rejection of proposed changes in a referendum. However, substantial progress has been made toward institutionalizing comprehensive performance measurement systems Citywide, in improving budget monitoring systems, and in improving the procurement system.

As the original Plan proposed, a number of initiatives to improve the efficiency of the City workforce have been implemented, such as elimination of inefficient work rules, more flexible scheduling, and broader job descriptions. Significant savings have been achieved through contracting out certain functions, as the original Plan proposed, although numerous functions cited in the original Plan as candidates for contracting out have not been considered to date. The original Plan also proposed creating a Productivity Bank, to provide an institutionalized mechanism to finance projects that increase revenues or reduce costs. This proposal has been implemented.

Some initiatives the original Plan proposed have not progressed, such as an initiative to coordinate the efforts of City housing agencies and consider a change in laws to create a single housing agency. Also, standard routes for trash collection trucks still have not been implemented.

With respect to personnel initiatives, longevity pay has not been eliminated as proposed in the original Plan. Benefits costs reductions have been achieved, although many measures proposed in the original Plan were not implemented, such as requiring co-payments, eliminating retiree and school crossing guard benefits, consolidation of the five health care programs, and elimination of legal services benefits. Overtime costs have been reduced through the elimination of holidays and reduction in sick leave time, although not to the extent the original Plan projected. Further reductions in overtime and sick leave are needed.

The original Plan cited the problem of a high debt burden, which continues to be a problem. Total City and PICA debt service are estimated at approximately 10.7 percent of City and PICA tax revenues.

Concerning initiatives the original Plan proposed with respect to the Department of Human Services, initiatives to reduce obligation growth, and increase revenues from Title IV-E, Act 148, and divert funding to Medicaid have been successful. Further reductions in the rate of obligation growth are needed, however. Some progress has been made on fundamental changes in service delivery, but much more is needed if DHS cost growth is to be reduced over the long run.

The original Plan included an initiative to reduce non-mandated Department of Public Health costs. While Medicaid revenue to the District Health Centers has increased and net costs of the Philadelphia Nursing Home have been reduced as a result of contracting out operations of the facility, net costs of the overall Department of Public Health have not been reduced since the time of the original Plan.

Within the Fire Department, Class 100 costs have been reduced through lower entry-level salaries, as the original Plan projected. Net EMS collections have increased, but not to the extent projected in the original Plan. An adverse arbitration award, which did not relieve the City from restrictive staffing-per-vehicle ratios, has driven Class 100 costs over projected levels.

Within the Department of Public Property, savings have been achieved as projected from privatizing custodial services. Net revenues from a per telephone line charge to fund 911 services have exceeded original Plan projections.

Within the Streets Department, savings have been achieved from implementing new waste disposal contracts and closing City trash transfer stations, as projected in the original Plan. However, based on recent Quarterly City Managers Reports, the impact of this initiative is not clear. Private alley lighting has not been discontinued, as the original Plan projected. In fact, over $10 million in Capital Program funding has been designated to finance modernization of alley lights throughout the City. Mechanical brooms have been purchased to reduce the employment of “blockmen.” However, the savings have been below original Plan projections, due to an arbitration ruling mandating reinstatement of some blockmen positions.

The original Plan projected savings from greater coordination between the Fairmount Park Commission and the Recreation Department, with respect to maintenance, fleet, and assignment of properties. This initiative has made virtually no progress.

The Law Department implemented an original Plan initiative to automate and increase staff in the Enforcement Division. Department collections data suggest this initiative has been successful in increasing revenue, although the recent declines in departmental collections suggest that future gains may be smaller. Another original Plan initiative, Law Department office consolidation, has not occurred to date.

**General Fund Revenues**

Total FY96-FY2000 Plan General Fund revenue projections appear reasonable.

Projections of non-tax revenues generally appear reasonable. Key assumptions include additional revenues from payments in lieu of taxes from non-profit organizations and fee increases, PGW revenues of $18 million annually, receiving approximately $4 million in annual SEPTA debt service reimbursement, and increases in County Health Act revenues, District Health Center Medicaid revenues, State Act 205 pension aid, and Utility Tax refund revenues. The most significant non-tax revenue risks relate to estimates of DHS Revenues from Other Governments.

The FY96-FY2000 Plan-projected General Fund tax revenue growth rates appear slightly aggressive, but these growth rates are calculated from a FY95 “base” tax revenue projection that appears somewhat conservative. As result, overall tax revenue projections appear reasonable.

A major risk with respect to the Plan tax revenue estimates is that a national recession during the Plan period could, at least temporarily, reduce growth rates significantly below Plan-projected levels. Also, the Plan assumes that delinquent tax collections will remain at current levels, which are very high compared to historical levels. Thus, the Plan is based on the assumption that revenue initiatives will continue to produce substantial delinquent tax revenue from better collection of delinquent taxes from currently registered taxpayers and continued discovery of a significant number of previously unregistered taxpayers.

The Plan projects $125.7 million in revenue from a Riverboat Gambling Wagering Tax in the FY97-FY2000 period, which is highly speculative, due to implementation hurdles, such as passage of State legislation and a possible State or local referendum requirement, and questions about the level of tax revenue that would be generated. The risk that these revenues may not be received as projected is offset by the fact that the Plan assumes that the proposed tax reduction will not be instituted if riverboat gambling is not legalized, absent other improvements in City finances that would make it possible to institute the tax cut without riverboat gambling revenue. The impact of the projected Wage Tax cuts projected for FY97-FY2000 is approximately equal to the projected Plan revenues from Riverboat Gambling.

There are also PICA Staff concerns about the Plan's estimates of the impact of the proposed tax reduction and restructuring. Some significant assumptions were made in estimating the effect of the tax changes, particularly with respect to the Business Privilege Tax. Only time will tell if those assumptions were correct.

**Obligations of Principal Operating Departments**

Department of Public Health obligations are projected to increase at an average annual rate of 1.2 percent over the FY96-FY2000 period. The obligation projections appear reasonable in relation to departmental revenue projections.

DHS obligation projections increase significantly more rapidly than those of other departments, reflecting increased staffing for decentralized offices, Family Centers, and increased social worker to case ratios, and increased purchased service costs for adoption subsidies, services to children in their own homes, day care, and medical-MH/MR services. Due to deceleration in growth rates in recent months, actual growth is likely to be lower than projected. Projections of Federal Title IV-E and State Act 148 revenues appear reasonable in relation to departmental obligation projections. PICA Staff is concerned, however, about the projected Federal Title IV-A revenue projection which appears aggressive in relation to obligation projections. The Plan projection of this new revenue source is speculative due to the lack of a collection track record. The impact of Federal welfare reform on Title IV-A and Title IV-E revenues is also uncertain.

At the request of PICA Staff, to reduce the risk to the Plan due to the uncertainty of the projected Federal DHS revenues, $20 million in annual revenues and obligations were moved to the Grants Revenue Fund for the FY97 to FY2000 period.

Fire Department obligation projections increase 4 percent from the projected FY95 level to the projected FY2000 level. FY95 Class 100 expenditures are projected to be over budget as a result of water rate changes, increased EMS services, and unanticipated costs from the 1993 contract arbitration award.

Current FY95 Fleet Management obligations projections are over original projections due to higher than expected salary costs and automotive parts purchases. The Plan projection of Fleet Management vehicle acquisition costs is $16.5 million in FY96, and grows to $20.4 million in FY2000. Vehicle acquisition cost projections in the Plan are a source of some concern since there is no detailed underlying analysis to substantiate these projections.

The Plan Police Department obligation projection assumes additional annual operating costs of $1.1 million for a new helicopter unit. Due to cuts in State capital funding for helicopters, the status of this unit is unclear. Another key Plan assumption is additional operating costs for additional communication dispatchers. The Plan also commits the City to expanding uniformed Police personnel by 753 over the Plan period through Federal Crime

Bill funding, and continuing to staff these positions after Federal funding has terminated. This commitment will have substantial fiscal consequences over the Plan period.

Department of Public Property obligations are projected to increase significantly in FY96 due to a new custodial and maintenance contract for the Curran Fromhold Correctional Facility. Notable Plan projection assumptions are a phasing out of vehicle leasing costs, flat utility costs, and declines in space rental costs.

**Major Areas of PICA Staff Concern**

With respect to the Department of Human Services, a major concern is whether the State will provide Act 148 funding for the variety of service enhancements and reforms that DHS has proposed for FY96. DHS has proposed decentralizing the location of social workers to offices throughout the City, more emphasis on preventive services by expanding the Family Centers and purchased services to children in their own homes, and changes to per diem rates paid to contracted service providers. Some of these changes are important to overall departmental reforms and whether they will receive State funding through Act 148 is a major issue. PICA Staff is also concerned about the impact of Medicaid managed care on the Department, and about continuing disagreements with the State over the interpretation of Act 30, which governs State funding of children and youth programs. Another PICA Staff concern is projections of Federal revenues, which may not be received at Plan-projected levels due to Federal welfare reforms, and also because there are difficulties in accurately estimating Title IV-A revenues due to the lack of a track record in receiving this new revenue source.

There are two major PICA Staff concerns with respect to the Department of Public Health. The first is the impact of the Governor's proposed changes in Medicaid reimbursement procedures for long term care facilities on reimbursements to the Philadelphia Nursing Home, and the net costs to the City under the contract with the private operator of the Home. The second is the potential impact of cuts in Federal and State funding for DPH programs, and whether the Department can absorb significant cutbacks in grant funding without the use of additional local funds.

With respect to the Fire Department, mandated staffing levels make it difficult for the Department to control overtime costs. Overtime costs are projected to be $2.3 million over budget in FY95. The Department is relying on cost savings in other areas to minimize the effects of overtime cost overruns on its total budget. However, the Department will continue to be susceptible to cost overruns if these savings are not realized.

With respect to the Police Department, there are two separate challenges to the City's liability for overtime costs in relation to new schedules implemented in 1990. While the City is optimistic it will prevail in both matters, there is a potential one-time liability to the City of $42 million with additional annual overtime costs in the future. These costs are not envisioned in the FY96-FY2000 Plan. Such a liability clearly would affect the overall General Fund budget adversely.

In the Prison System, projections of food service costs are a source of concern due the projected transition to a new system of food delivery with the opening of the new Curran Fromhold prison.

With respect to the Department of Public Property, PICA Staff is concerned about the Streets Department's need for improved communications systems to improve trash collection efficiency. The delay in implementing the new Citywide communications system has been a problem, and the Departments of Public Property and of Streets are not apparently in agreement over the best interim solutions. PICA Staff is concerned over the lack of centralized leadership over decisions concerning the City's mobile communication system. Another concern is the lack of consistent reporting on the use of proceeds from the 911 telephone user charge.

With respect to the Streets Department, a major problem is high sick leave usage in the Sanitation Division which contributes to increased overtime costs. The source of the problem is twofold, according to the Department. First, sanitation employees are exposed to inclement conditions so they are more susceptible to illnesses. Second, misuse of overtime remains high in the Division. The Department needs to develop and utilize enforceable procedures to manage sick leave usage and help control overtime.

Since the inception of the Office of Fleet Management, the City's Fleet Manager has stated that a key to the agency's success is the establishment of a centralized fleet repair facility. The delay in locating a centralized fleet repair facility continues to be costly to the City in terms of increased overtime costs and reduced ability to properly control inventory. According to the Office of Fleet Management, substantial inventory losses have occurred. PICA Staff encourages taking all the necessary steps to make improvements with regard to improving inventory control, including establishing a centralized fleet repair facility.

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## CAPITAL PROGRAM OFFICE

Primary Areas of Concern

- o Inadequate project information and control system to keep departments and senior management apprised of project status
- o Lack of Critical Path Management
- o Lack of Preventive Maintenance Programs
- o Relationship to the Strategic Plan

Introduction

For the first time in recent years, the City of Philadelphia anticipates independently entering the capital market in FY96 to issue general obligation bonds to provide funding for its capital program. The FY1996-FY2000 Five Year Plan anticipates that the City will issue bonds to provide funding for a FY96 Capital Budget totaling $152 million. The bulk of the contemplated FY96 projects are in Prisons (a new House of Corrections), Commerce (Avenue of the Arts), Fleet Management (underground fuel tanks and centralized facility),Public Property (City-Wide Radio System), and Recreation (including Veterans Stadium).

In previous reports, PICA Staff has criticized the City Administration for being a model of inefficiency in planning and monitoring annual capital budgets. A sampling of our previous concerns are revisited in this report.

**Inadequate Project Information -- *In the past the City has been unable to provide departments and senior management the tools to properly monitor projects***

We earlier expressed our disappointment with the quality of information the City provided to support requests for encumbrances against PICA funded capital projects. Requests were found to have incorrect descriptions of work being performed at some facilities, inaccurate accounting balances, and schedules that incorrectly identified the current stage of the project. PICA raised its initial concerns with the anticipation that the City would strive for improvements for the City's own internal control purposes as well as to satisfy PICA qualms.

While PICA remains wary of the City's ability and willingness to properly manage capital funds, the City, in the FY1996-FY2000 Five Year Plan, appropriately identifies the following improvements to its capital program management:

- o Establishing new project management, scheduling, and monitoring systems that are enabling the City to track the implementation status of each capital project,

- Installing a new automated accounting system in conjunction with FAMIS that collects detailed information about each project, enabling the City to analyze and track budget, encumbrance, and expenditure information by categories such as facility, funding source, or type of improvement, and
- Having departments submit project requests and information on computer disks with an improved level of detail in order to facilitate communication between the Capital Program Office and departments using capital funds.

PICA Staff, while pleased with the City's progress in this area, remains cautious because problems within the capital program are historically institutional and automation alone will not address its concerns. As the City's CIO has stated "automation without a strong foundation only produces sloppy work faster".

**Critical Path Method -- *Organized programs are still lacking in the City's capital program***

In previous reports PICA Staff has stated that "much of the capital program management problem appears to result from non-use of state-of-the-art project management skills and techniques by City architects and engineers". In response to these concerns both the Capital Program Office and the Department of Public Property gave PICA Staff assurances that both the City and its vendors would incorporate Critical Path Management (CPM) methodology in future projects.

To PICA's dismay and despite these assurances no significant progress has yet been made in this area. In recent meetings with City Staff, PICA Staff was advised that the majority of City projects do not use this management tool, and there were no immediate plans to do so.

PICA Staff continues to believe that if CPM was used by the City's architects and engineers the City's capital program would be significantly more efficient. PICA Staff will continue to focus on this area.

**Preventive Maintenance Programs -- *While improved, they still fall short of what is needed***

In the past PICA Staff has been extremely critical of the City's preventive maintenance program for its facilities. A study performed by the City's Controller's Office as of April 17, 1991 stated that of 127 buildings inspected, 32 (25%) were considered to be in poor or hazardous condition. It had been the City's practice to overlook daily maintenance and routine repairs in favor of new construction, using capital dollars rather than operations dollars. PICA Staff continues to encourage the City to set aside operational funds and implement preventative maintenance programs that extend the life of all facilities, especially projects PICA recently financed.

While much remains to be done the City has made significant progress in this area. An example of such progress is in the Department of Recreation. The Recreation Department Commissioner has advised PICA Staff that, along with hiring eleven additional maintenance personnel, the Department has instituted preventive maintenance programs in the following areas: indoor/outdoor lighting, roofing and heating, and plumbing for the recreation centers lavatories. The Commissioner indicated that the programs were running well but the lack of sufficient funding for items like ladders and appropriate vehicles hinders performance. PICA Staff is pleased to see the start of such progress and hopes to soon see these types of programs used City-wide.

**Strategic Plan --** ***The City continues to prepare capital budgets without the guidance of a strategic plan***

As in previous years the City has prepared its FY96 capital budget without the benefit of a comprehensive strategic plan which would assess each facilities condition or its projected long-range purpose or use. Historically, this has encouraged the inefficient management and spending of capital funds.

As a part of this year's Five Year Plan the City has included as an appendix, a comprehensive first stage strategic plan entitled "Philadelphia 2000". Within this plan the City has a section titled "Invest in Infrastructure and the Physical Environment" which spells out the following areas which it hopes to address:

- Increase capital investment in the City's existing infrastructure and public facilities and improve preventive maintenance to reduce the need for future rehabilitation;

- Target more resources to stabilize neighborhoods beginning to show housing deterioration and abandonment, while retaining the City's primary commitment to rehabilitate its most blighted neighborhoods and provide housing assistance to its lowest income residents and the homeless;

- Revitalize the Philadelphia Housing Authority (PHA) to reduce the vacancy rate and maximize the availability of well maintained housing units; and

- Expand demolition and "clean and seal" programs for imminently dangerous properties and houses used for illegal activity, while increasing efforts to reduce the number of historic and other properties that are allowed to deteriorate to dangerous levels.

While PICA Staff applauds this first attempt toward establishing capital goals and strategies, we still feel this first stage plan falls short of dire needs.

The City's strategic plan indicates that one-half of all free libraries were built before 1923. The City also indicates that due to the most recent "cash-crisis" maintenance for these buildings has been limited and consequently some of these buildings have "deteriorated to dangerous levels." As a result the City has pledged to spend more money on these facilities.

In previous reports, PICA Staff has criticized the City for not focusing on preventive maintenance, and we are glad to see the City begin to address this area, but PICA Staff has also criticized the City for not reviewing the need for their many facilities and the strategic plan does not presently address this issue. The City, in the FY92-FY96 Five Year Plan, made the following observation:

> "Currently, 12 stations (fire) are inefficiently located as a result of shifting demographics and could be combined into six stations. These consolidations would have to be located strategically according to the demographic make up of the City. In some instances, this would require the construction of new facilities. Each new station would involve construction costs of roughly $1.2 million. However, it is estimated that, through consolidation, the Department would save from $.9 to $1.2 million in the first year alone."

PICA Staff finds it disturbing that the issue of facility demographics has not been seriously reviewed by the City. While decisions as to use/closure, location/relocation, consolidation and disposition of surplus facilities are controversial and politically charged, the City's Administration will have to start to deal with these types of issues. It seems ludicrous for the City to initiate a strategic plan process that is supposedly to take the City into the year 2000 and which contemplates spending approximately $125 million annually on capital projects without consideration of the City's ever changing demographic make up.

## STRATEGIC PLAN

The Strategic Plan document included as an appendix to the FY96-FY2000 Five-Year Financial Plan provides a clear and concise description of the issues City government faces and the strategic direction in which the City as a whole should move. However, this represents only the first of two phases of the strategic planning process envisioned by the City, and in some respects the easier phase. The document provides a Citywide Strategic Plan, which in Phase II of the strategic planning process must be used as a frame of reference by City departments to produce their own departmental strategic plans to conform with and implement the Citywide plan. The strategy developed must then be incorporated into program, financial and budgetary decision-making. Although the process is far from over, the production of the Citywide Strategic Plan by the City is a major step forward.

The Strategic Plan is divided into ten sections, each of which contains several strategies. For many strategies, the Strategic Plan lists several specific action steps that will implement the strategies.

Some of the elements of the Strategic Plan are actions that the Rendell Administration has been pursuing for the past three years, and have been incorporated into the Five-Year Financial Plans presented to date. Other elements are new, in part because they have less direct General Fund financial impact, but they are nonetheless important to the long-term health of the City. The discussion below highlights some of these new elements and their relationship to the FY96-FY2000 Plan.

*Squeeze Every Nickel*

The strategies under this section have been major elements of Five Year Financial Plans in the past. They include: targeting historically out of control costs, pursuing full tax and fee compliance, and working for efficiency and productivity gains. While the City has made considerable progress in addressing these three areas, continued efforts are needed to control rapidly increasing expenditure categories, and to strive for continuous efficiency gains. Initiatives to improve revenue collection are still in progress. This section states that “now that an era of adversarial restrictions is ending, the challenge is to redefine a new labor-management partnership based on expanded worker involvement and teamwork.” Such a new labor-management partnership would greatly assist in efforts to increase productivity while improving compensation and working conditions for the workforce.

One strategy under this heading represents a new element that has not figured prominently in past Five-Year Financial Plans, evaluating opportunities to divest from select services. PICA Staff believes that this element should receive major emphasis under the Strategic Plan in the years to come. The Plan notes that “the City now fulfills some roles that are properly the responsibility of other governments, and provides some services that could likely be sustained by private sector support.” Items the Plan mentions in this regard include phasing out operating subsidies to some cultural institutions, which is an element of the Five-Year Financial Plan; reexamining funding and administrative roles of the City in county functions, an area which can only be addressed in conjunction with the State; as part of departmental strategic efforts, charging every department with identifying services that are inappropriate to the departmental mission, such as Police Department non-emergency transportation of citizens to hospitals; and transfer of the Philadelphia International Airport, the Water Department and Philadelphia Gas Works to the private sector or public authorities. These areas are among the most important strategic issues the City faces and the strategic planning process, as it continues into the phase of department planning, should make these issues a major focus. The City's challenge is not only to provide services efficiently, but to provide the right mix of services. This may require divestment of some services as well as changes in service levels or providing new services where appropriate.

*Energize the Economy*

This section is essentially a summary of the Economic Stimulus Program (ESP). Including it within the Strategic Plan is useful, however, as an indication that the Economic Stimulus Program should be pursued within the context of the goals of the overall Strategic Plan.

*Cut the Cost of Doing Business*

This section incorporates other strategies to improve the economic performance of the City. Two strategies included in this section, reduce taxes and rationalize and simplify the tax structure, are not new to this Strategic Plan. Progress on tax simplification and rationalization has already taken place in recent years, with implementation of recommendations of the Joint Administration/City Council Select Committee on Business Taxes. The FY96-FY2000 Plan proposes measures to reduce taxes and further rationalize the tax structure. PICA Staff believes that further City tax reduction and restructuring of City taxes to promote a more efficient and fair tax system are important actions needed to promote economic development. The City imposes a number of taxes that are hard to justify on the basis of any criterion of tax efficiency or fairness. The "Squeeze Every Nickel" section notes that the City will seek the repeal of inefficient nuisance taxes.

Other strategies under this section attempt to improve the economic development of the City by addressing factors other than taxes that influence business location, such as service quality, taxes, regulations, insurance costs and utility costs, some of which are not directly the responsibility of City government. One strategy, to make City government more business-friendly, is in part already being pursued, through such steps as an initiative to allow faster permit processing through the Department of Licenses and Inspections. The Plan also includes action steps to implement this strategy: improved training for personnel, consolidation of fee payments so payments can be made at one time and in one place, and assignment of Commerce Department personnel to individual businesses to help guide businesses through various City processes. Another strategy, which has not received prominence under previous Five-Year Financial Plans, contemplates working to reduce business costs that are not directly the result of City policy, such as State taxes, utility rates, workers compensation and insurance rates.

*Make Public Education the Preferred Education*

Initiatives relating to Public Education have not been incorporated into Five-Year Financial Plans or the Economic Stimulus Plan to date. Integration of the School District into the City's Strategic Plan is essential to the City's economy and long-term health, both because of the great importance of the School District as a major taxing and service providing agency and because of the trend toward more integrated service delivery among City agencies and the School District.

PICA Staff's concern is that some of the strategies will require additional funding. One such strategy is to improve school readiness by increasing Head Start, pre-school and full-day kindergarten. The Plan states that the City will work to achieve changes in State reimbursement rates for kindergarten to fund this initiative. Another strategy that requires additional funding is to improve support services through Family Centers and Community Schools. The source of funding for Family Centers is uncertain at this time since State funding for Family Centers through DHS Act 148 funds has not been approved.

Other strategies include support the Superintendent's "Children Achieving" agenda, improving School District efficiency. The Plan states that the City will continue to pursue additional funding for the School District first through improved efficiency, and second through increased State funding for the district, but that additional burdens on the City's general tax base should be avoided. PICA Staff would note that through the imposition of PILOTs for non-profit organizations and the institution of the Liquor Tax, the City has recently increased the percentage of its tax base that is devoted to the School District. In the long term, the resource needs of the School District and the extent to which the City tax base will have to meet these needs is a major PICA Staff concern. At the same time, viewing education needs as simply a matter of increasing programs, decreasing student-teacher ratios, and increasing funding without fundamental changes will not be sufficient.

Another strategy is to increase accountability through two action steps. The first action step is to change the Charter to reduce the time before a newly-elected Mayor can appoint a majority to the Board of Education, which is currently four years. The second action step is to encourage the School District to publish performance measures on a school-by-school basis.

*Strengthen Families*

This section includes strategies that would promote a more comprehensive and coordinated approach to provision of social services that would be more effective in preventing problems rather than simply dealing with their effects. The first action step is that "the City will shift as many of its limited resources as possible toward the prevention of health and social problems." The current Five Year Plan and previous Plans have emphasized prevention of social problems in Department of Human Services programs and Homeless Services programs. This strategy would require a more comprehensive approach to prevention across all services, and program evaluation to determine the most effective approaches.

Another action step is to develop Family Centers and Youth Access Centers to provide coordinated human services, health, literacy and education programs for children and families. PICA Staff is concerned about the availability of long-term funding for these programs.

The third action step is to develop “Community Schools” in collaboration with the School District that will provide a variety of services in school buildings that are open at night, on weekends and during the summer. This will require new funding. The City will also collaborate with the School District to enable private providers to operate afterschool childcare centers in school buildings. The City will also shift hours of operation of parks, recreation centers and libraries towards evenings and weekends to make services more accessible.

Another strategy is to develop a Children and Families Strategic Plan through the Children and Families Cabinet. This Plan would coordinate education, health and human services provided to children, families and communities by sixteen City agencies and the School District, to “better serve each child by strengthening families in the communities where they live and by enabling the various agencies to work together to provide the needed array of services.” PICA Staff notes that the Homeless Programs section of the FY96-FY2000 Plan states that “during the next few years, homeless services must be integrated into an overall City service strategy for low-income persons.” Such a strategy would clearly need to be related to the Children and Families Strategic Plan. Strategic planning for health and social services provided to children and families, and to low-income residents of the City generally, is needed because of the fragmented nature of these programs and the large number of agencies that deliver them. Progress in developing and implementing such a Plan would be very significant. Further, the potential movement at the Federal level toward providing more funds for health and social services on a block grant basis could facilitate a more strategic approach to health and social services policy by the City government.

*Mobilize Community Involvement*

This section includes several separate strategies, linked by the common idea of improving residential life. The first is a strategy to promote volunteerism, and citizen participation. The Strategic Plan notes in the “Squeeze Every Nickel” section that promoting volunteerism, which has already had positive results in many areas of City government, will not only result in financial savings but will also help build strong communities.

Another strategy would target City services into blighted areas through the Partners for Progress program, in a manner that will help citizens gain a sense of commitment to their community. Another strategy is to stabilize and rehabilitate neighborhoods through the Philadelphia Plan, a partnership between corporations and community development corporations. Another strategy would build leadership capacity in neighborhoods by supporting Neighborhood Advisory Councils and Community Development Corporations through technical and leadership support and training. Another strategy is to promote greater harmony within and across neighborhoods, through agencies such as the Human Relations Commission, and through equitable resource distribution by City government.

Most of these programs are elements of the Five-Year Financial Plan or the Economic Stimulus Plan. The important element of including them in the Strategic Plan is that it clarifies the role of these various programs in improving community life. It is appropriate that the Strategic Plan focus on quality of residential life in the City as well as business conditions, since Philadelphia's economic and financial future depends on its ability to attract residents as well as businesses.

*Reduce Crime and the Fear of Crime*

This section includes initiatives to prevent and more effectively deal with crime. Strategic coordination is particularly important in this area due to the large number of City agencies and programs that address crime. The first strategy under this section is to expand community policing, Town Watch and anti-drug programs, and expand the number of police on the street through additional Federal Crime Bill funding. These strategies have important financial impacts which have been incorporated into the FY96-FY2000 Plan.

Another strategy is to expand positive alternatives to crime and drugs by providing recreation and cultural programs and conflict resolution training. PICA Staff is concerned about the availability of funding for these programs, particularly if Federal Crime Bill funding for these purposes is reduced.

Another strategy would institute a more effective incarceration policy by: ending the prison "cap;" bringing on-line new facilities such as the Curran Fromhold Prison, the Criminal Justice Center, and a replacement for the House of Correction; instituting new information systems and joint programs with the courts to speed pre-trial processing; and expanding alternative sentencing under standards that do not put communities at risk. These programs also have important financial impacts, and PICA Staff continues to be concerned about the extent to which these strategies can be fully implemented within the financial projections in the FY96-FY2000 Plan.

*Invest in Infrastructure and the Physical Environment*

Under this section, the first strategy is to expand and professionalize preventive maintenance for current City facilities, and increase capital investment in those facilities. The City has increased levels of operating preventative maintenance funding in recent years, although PICA Staff remains concerned about whether the City is spending at a level adequate to maintain its vast infrastructure. A more coordinated and efficient unified Citywide preventative maintenance program is still needed. The Strategic Plan also includes professionalizing preventive maintenance, a goal that the City has indicated it wishes to pursue for several years. PICA Staff is concerned that progress to this end does not appear to be occurring.

The level of capital investment has increased in recent years through PICA capital borrowings, and it appears this trend will continue, based on the City's FY96-FY2001 Capital Program. In the opinion of PICA Staff, a continued high level of capital investment would only be appropriate if the Capital program were based on a long term Strategic Plan for City government as a whole and for City departments. PICA Staff's most fundamental concern about the City's capital program is that decisions about capital spending for facility construction, renovation, and closure and ongoing spending for maintenance should be based on a strategic plan regarding what services the City wants to provide and where, and what configuration of City infrastructure will support the most efficient delivery of those services. The Citywide Strategic Plan, as well as strategic plans prepared for individual departments as part of Phase II of the Strategic Planning process, should be used as the basis for the development of the Capital Program. Until such plans are available to provide a basis for capital spending, PICA Staff is concerned about the continued high level of spending projected for the near future.

The City is in the process of preparing facility condition assessments for several departments. These studies should assist in making decisions with regard to the maintenance and rehabilitation of present infrastructure. What these studies will not address, however, and what a strategic plan should address, is what facilities the City should have to provide desired services efficiently and effectively.

Other strategies in this section are: to improve allocation of housing resources by targeting more resources to neighborhoods beginning to show housing deterioration; to continue to revitalize PHA; and to continue demolition and Clean and Seal programs, while increasing efforts to reduce the number of properties allowed to deteriorate to dangerous levels. The Plan projects L&I demolition costs in FY96 at no increase from the FY95 level, and obligations in FY97-FY2000 increase at 1.5 percent annually, which should be adequate to continue demolitions at approximately their current level.

*Emphasize Customer Service*

This section embodies the City's commitment to strategic planning as a way to refocus the efforts of City government to emphasize customer service. Under Phase I of the City's strategic planning process, a Citywide Strategic Plan was produced. Under Phase II, every department and key interagency group will refine and develop its own strategic plan. The process will be focused on identifying customers and on meeting their needs as efficiently and effectively as possible. Several departments have developed strategic plans in recent years, and all departments will be expected to develop new plans or update old plans to a point consistent with the Citywide Strategic Plan. Development of these plans is critical to implementation of the general strategic goals that have been developed in the Citywide strategic plan. Together with service level information, development of departmental strategic plans will provide the basis for budgetary decision making that reflects the considered priorities of the City and is based on the information necessary to see that those priorities are achieved as efficiently and effectively as possible.

Another strategy included in this section is adopting departmental service goals and standards, to measure progress, better target resources and establish clearer expectations. Comprehensive, reliable and regularly-reported service level information is needed along with financial information to allocate resources efficiently and in line with the City's priorities. The City has recently made considerable progress toward developing performance measurement processes, and is to be commended for this progress.

Another strategy in this section has not been mentioned in previous Five-Year Financial Plans. This is to build a long-term capacity for leadership through the establishment of a new Municipal Management Intern program. Under this program, recent graduates of masters level programs will commit to two-year internships as management or budget analysts, and will then be eligible for placement in permanent management posts across City government. The program is designed over the long-term to strengthen middle management skills, and develop the next generation of senior management. Building a long-term capacity for leadership throughout City government is critical to maintaining and extending the improvements in financial management, productivity and service delivery instituted in recent years.

A final strategy is to invest in improving City facilities, to improve public service and employee morale.

*Expand Intergovernmental Partnerships*

This section of the Strategic Plan describes key issues with respect to the Federal and State government, and other regional governments. Under the Strategic Plan, the City will promote an agenda for the Federal government that will find ways to support the economies of cities without significantly adding to the national debt, such as creating a preference for location and relocation of federal facilities in distressed urban areas, expanding federal tax incentives for urban development, eliminating unfunded mandates, creating incentives for regional cooperation, lifting restrictions on community-based housing development, and addressing urban environmental challenges.

With respect to the State government, the Plan indicates the City will work toward full State funding of county functions. Support of county functions in Philadelphia requires a extremely high tax effort of local residents compared to residents of other counties in the State. This problem needs to be addressed, perhaps in a way that will promote improved efficiency. With respect to regional governments, the City will work to develop regional cooperation concerning airport governance, arts and culture, and environmental planning.

Issues of federal, state and regional intergovernmental cooperation are among the most important issues affecting the future of the City. It is important that these goals are placed within the context of a Strategic Plan containing a long list of ambitious targets that

City employees plan to achieve through their own dedication and hard work. On the basis of the performance to date, but only if further improvements such as those outlined in the Strategic Plan are pursued with the same degree of relentlessness that the City has demonstrated to date with regard to its financial problems, the City can legitimately request that other levels of government consider funding and program changes that will reduce the financial pressure on the City.

## Economic Stimulus Program

The Economic Stimulus Program (ESP) was first presented as part of the FY95-FY99 Five-Year Financial Plan as a three year program covering calendar years 1994 to 1996. While the program did involve some new initiatives, the primary significance of the ESP was as an effort to proactively manage the City's economic development programs in a coordinated way to produce the maximum effect on the City's economy. Economic decline in the City has been a major factor contributing to the City's recent financial problems. Reversing the City's declining economic trend lines through development of a proactive economic development strategy is very important if the City's financial stability is to be maintained over the long term.

In the FY96-FY2000 Plan, the amount of ESP funding attributed to some programs has increased beyond the amounts included in the FY95-FY99 Plan, and some additional programs have been included in the scope of the ESP, resulting in an increase in the total public and private funding included in the ESP for the 1994-1996 period. The FY96-FY 2000 Plan indicates that actual pace of spending for calendar 1994 in many cases exceeded the original projections in the FY95-FY99 Plan.

The ESP receives significant funding from State and Federal sources. Substantial allocations of local capital spending are also included. In addition, the ESP includes several programs that are projected to receive City operating funding. The ESP projects $30 million will be provided from the General Fund, during the three years of the ESP, to the Business Retention and Attraction Fund which provides flexible funding that can be used in conjunction with other State and Federal funds in providing incentives for businesses to locate or remain in the City. The Neighborhood Stabilization Fund is projected to receive, over the three year period of the ESP, $10 million in local tax source funding and $200 million from riverboat gambling franchise fees, and provide funding for site acquisition, demolition, and cleanup, to support potential commercial and industrial projects. In addition, $11.4 million in General Fund dollars are projected to be allocated to housing programs over the three years of the ESP.

*Problems with Reporting*

The "Economic Development" section of the FY96-FY2000 Plan and the recent publication of the first quarterly *Economic Stimulus Report* provide a great deal of information about the City's economic development activities. However, the data presented is sometimes not very clear, particularly in regard to its relationship to the City's operating and capital budgets. In both the Plan and the *Economic Stimulus Report,* information provided in tables concerning the sources and uses of funds for the individual component programs of the ESP is sometimes not sufficiently detailed to relate clearly to figures in descriptions of programs in accompanying text, or to figures in the FY96-FY2001 Capital Program document.

*Basis of Investment Decisions*

PICA Staff believes that major emphasis should be placed on basing resource allocation decisions within the ESP on evaluations of program effectiveness, so that the best possible results can be achieved with the limited economic development resources available to the City. Whether allocating investment dollars to retaining existing businesses or to industries and firms that might be attracted to Philadelphia, it is important that investments be based on program evaluation. Analysis of the comparative advantages and disadvantages of the City economy may also help guide investments to where they will be most productive.

A major portion of ESP resources are targeted to increase economic activity associated with conventions, tourism and regional visitors, and to support conversion of defense facilities to civilian uses. The remaining investments in the ESP do not appear to be targeted to any specific industries, although in some cases they are targeted to specific geographical areas, such as the Empowerment Zone areas. The Plan does not discuss the issue of program evaluation and its relation to the process of allocating resources among various components of the ESP, which raises a question about the basis for resource allocation decisions within the ESP.

*Tax Reduction and Restructuring*

The Economic Development Section of the FY96-FY2000 Plan presents the Rendell Administration's proposal to reduce and restructure taxes, and a discussion of the rationale behind the proposal. While not defined as part of the "Economic Stimulus Program", this proposal is a major component of the Administration's efforts to improve Philadelphia's economic performance. Tax reduction and tax restructuring are two of the most important issues that need to be addressed to promote economic development in the City. The proposal contains the following elements:

- A gradual reduction in the resident and non-resident rates of the Wage, Earnings and Net Profits Taxes over the next five years, reaching a 7 percent reduction in FY2000

- A gradual reduction in the rate of the gross receipts portion of the Business Privilege Tax over the next five years, reaching an 18 percent reduction in FY2000

- A change in the formula used to calculate the portion of a firm's net income and gross receipts that are subject to the Business Privilege Tax, which would double-weight gross receipts earned within the City

- A change in the interest rate charged by the City on late Business Privilege Tax payments, to conform with the State interest rate

The proposed tax reductions should begin to address two elements of the City's tax burden that have been identified as significantly higher than the average in competing jurisdictions, local business taxes and local personal income taxes. While these reductions alone will not bring Philadelphia to the level of many competitor locations in its suburbs or other cities, the reductions, if implemented as proposed over the five years of the Plan, would bring Philadelphia significantly closer to these competitors. Implementation of the tax cut signals that the City is committed to making Philadelphia taxes competitive and that the trend of increasing tax burdens in the City may not continue inexorably, but may in fact be reversed, if the City government maintains its commitment to reducing the cost of government over the long term.

The proposals for tax restructuring are consistent with recommendations made in 1993 by the Joint Administration/City Council Select Committee on Business Taxes. Further restructuring is likely to be necessary over the long term. There are a variety of recommendations made by the Select Committee which have not been implemented. Also, the City retains a number of nuisance taxes which generate fairly small revenues without clearly contributing to any criterion of tax efficiency or fairness. These taxes should be reevaluated.

Certainly, with regard to both tax reduction and tax restructuring, there is more the City needs to do, but the proposal contained in the FY96-FY2000 Plan, if fully implemented over the next five years, would be a very important step in the right direction.

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## Current Status of FY92-FY96 Plan's Management Initiatives

This section contains a review of key initiatives that formed a basis for financial projections in the Rendell Administration's first Five-Year Financial Plan, the FY92-FY96 Plan, (the "original Plan"), and their current status and future prospects. Also included is a review of key issues raised in the original Plan that needed to be addressed, and their current status and future prospects. PICA Staff undertook this review to illustrate at once how much progress has been made since the original Plan and how much there is still to be accomplished of the agenda laid out in the FY92-FY96 Plan.

### Management and Productivity

<u>Structural Changes</u>

The Management and Productivity section of the original Plan noted that reform was needed in "systems of government that are common to all departments." According to the original Plan, "the City's personnel practices make it impossible for managers to manage, and stifle employee innovation and initiative. The Charter unnecessarily restricts management's ability to make real change in operating departments. The budget process has no incentives for departments to innovate, or to save money. The procurement system is overly bureaucratized and slow. Work rules, often established by past practice, too often stand in the way of creativity and efficiency." The Plan noted that the Administration would seek reforms in these basic systems. The discussion below describes the achievements to date and the substantial challenges that remain with respect to reforming these basic systems of City government.

*Personnel Reforms*

The original Plan included an initiative to implement a merit-based performance evaluation system that would provide a basis for compensation, promotions and transfers. This is one of the more significant unfulfilled initiatives of the original Plan. The FY96-FY2000 Plan indicates that the Personnel Department's accomplishments since 1992 have been in the redeployment of City workers displaced by competitive contracting, implementation of legal mandates, and promoting workforce diversity. The Department has also assisted in improving labor relations and streamlining labor contract administration through negotiation of a master DC47 agreement, efforts to improve the labor relations skills of departmental managers, and improvements in processing of employee grievances. The Department has also worked to make the existing civil service system more efficient, through improved examination processing and changes in personnel classifications. Personnel classifications have been updated or eliminated, new classifications have been created, and overly specialized classifications have been consolidated so that the personnel classification better reflects current needs of the City. However, basic structural reform in the personnel system so that hiring, promotion, and compensation under the civil service system will promote performance goals, has not been achieved.

*Changing the Charter*

A Charter Revisions Commission was created, and it developed a comprehensive set of reform recommendations that would have made many structural changes to City government. However, the package of recommendations was defeated in a referendum. At the earliest appropriate time, PICA Staff recommends that revised recommendations should be revisited.

*Budget Process/Performance Measurement*

The City's current progress in developing a system of performance measurement will be a key element in achieving the original Plan's goal of budget process reform to promote the incentives of departments to innovate, or to save money. The institution of the "Departmental Service Delivery Report" as part of the Quarterly City Managers Report, beginning in the Quarterly Report for the first quarter of FY95, is a sign that the City is making significant progress toward developing a comprehensive system for measuring the performance of City government. The report includes about 150 performance indicators from 32 City agencies. In the future, measurements from additional departments are expected to be added to the report, and measures provided by other departments are expected to be improved. In the fall of 1995, the City plans to publish the first annual Mayor's Services Report, which is to include discussion of service levels and trends. In addition, service level trend information has been included in the FY96-FY2000 Plan, the first time such information has been included in a Five-Year Financial Plan. PICA Staff applauds the progress the City is making in performance measurement.

PICA Staff believes that institutionalizing procedures to produce comprehensive, reliable and regularly-produced performance indicators would be a very important, positive, long-term, structural change in City government. As the Plan notes, performance measurements provide many benefits, such as assisting managers in assessing service efforts and accomplishments, establishing benchmarks for performance, providing greater accountability, improving the ability of government to make well-informed decisions about service levels and budgets, and providing the opportunity for City managers to be held responsible for attaining service delivery milestones as well as financial targets.

In the opinion of PICA Staff, in order to promote the incentives of departments to innovate and save money, one of the goals of the original Plan, performance measurement needs to be combined with a compensation system that rewards performance and a budget system that allocates resources strategically. Performance measurements for programs and organizations should be used to make budgets that allocate resources efficiently and in line with the City's priorities. Performance measurements for organizations and individuals should be used to provide the foundation for a pay for performance system. Unless budgets and pay plans are used to reward the programs and people that perform, performance measurement will not have much effect. The combination of these elements is essential to improving the two bottom lines that matter to the public, service levels and tax levels, the two results that the Rendell Administration has repeatedly said must be improved to preserve the long-term health of the City. While the development of performance measurement is providing an essential foundation, to achieve the goal of the original plan to promote the incentives of the departments to innovate and save money, further progress is needed in using this information in budget making and in setting compensation.

Another key element of budget process reform is the system of budget monitoring instituted under the Rendell Administration. Under this system, monthly results are reported in relation to target budget plans and end-of-year projections are revised on the basis of those results. Results to date and updated projections are published in the Monthly and Quarterly City Managers Reports. The reports describe reasons for variances between projections and budget. These reports are a valuable tool for both the City Administration and PICA Staff in monitoring financial results and budget and Five-Year Financial Plan compliance on an ongoing basis throughout the fiscal year. Having accurate projections throughout the fiscal year also assists in the annual process of budget preparation and Plan revision.

*Procurement System*

With respect to the procurement system, substantial progress appears to have been made since the time of the original Plan. Public works bidding requirements have been changed to reduce barriers to competition and to ease administration for the City; the bid limit for small order purchases has been raised, and a greater portion of total purchasing is handled through citywide contracts for commonly used items. Privatization of services previously provided by the City print shop and procurement warehouse have resulted in improvements to procurement of office products and printing services. The City is in the process of implementing ADPICS (Advanced Purchasing and Inventory Control System), a computerized procurement system that will, according to the current Plan, "automate the entire procurement and inventory system of the City from initial requisition to final payment." The average processing time for all purchase orders has decreased from 89 days in FY92 to 64 days in the first quarter of FY95. The Plan projects further reductions in processing time for purchases. Further progress in implementation of ADPICS is a major future agenda item for the procurement system.

*Work Practices*

With respect to work practices, the original Plan also proposed the removal of antiquated work rules and past practices, the introduction of more flexible work schedules to make more efficient use of resources and also reduce overtime. The Plan notes that significant progress has been achieved in these areas. In the labor agreements with the City's four major unions, the City successfully negotiated for the City's first-ever management rights clauses, clearly establishing the City's right to use new technology, direct employees, and determine programs and organizational structure. As of November 1, 1994 departments have reported 154 significant completed changes in work practices, with 22 more changes now under consideration or implementation.

The City's right to use volunteers and other no-cost workforces has been clarified. Among the results of this have been the expanded use of volunteers at the Free Library, and use of National Guard assistance to clean and seal abandoned houses. Costly work rules such as the restriction on the use of power equipment by Fairmount Park seasonal employees have been eliminated. Civil service job descriptions have been broadened to provide for more flexible use of personnel. Managers have been given greater ability to modify work schedules. Among the results of this change is the ability to offer evening hours at District Health Centers without automatically generating overtime. The City received the right to civilianize 179 positions, so that desk jobs once filled by uniformed officers are now staffed by less expensive civilian employees. General Fund savings from labor initiatives, exclusive of competitive contracting and volunteer programs, is estimated at $3 million in FY95.

However, several goals of the original Plan with respect to work practices have not been implemented. These include: improved shift scheduling for police, which has not been implemented to date due to ongoing disputes with the Police officers union; more flexible vacation scheduling for uniformed services; and seasonal staffing in the Streets Department.

Competitive Contracting

A major goal of the original Plan was to inject competition into all levels of government. The original Plan indicated that the City intended to seek private bids for a number of services, which that Plan said may include: legal and debt collection services, building and grounds maintenance, Fairmount Park and Recreation Department facilities maintenance, fleet management and maintenance, Art Museum and other building guard services, Philadelphia Nursing Home and Riverview Home, data processing, trash collection, road and street maintenance, tree trimming and planting, and streetlight operation.

Since the time of the original Plan, 26 functions have been contracted out, and 2 functions have been analyzed for the potential benefits of contracting out but were retained in house based on the analysis. In addition, 27 other functions are currently listed in the Quarterly City Managers Report as functions that are being considered for competitive contracting. There are still a number of functions included in the original Plan as potential functions to contract out, but which have not been contracted out or are not under active consideration, such as building, grounds, and facilities maintenance, fleet maintenance, Riverview Home, trash collection, road and street maintenance, and streetlight operation. PICA Staff believes that there are still many functions that the City should consider for contracting out. The reduced financial pressure the City is now facing should not reduce the emphasis the Administration has previously placed on using contracting as a means to promote greater service delivery for each City dollar. Also, greater emphasis should be placed on refining and institutionalizing the process of evaluating costs and benefits of in house versus contracted production, to insure that competitiveness becomes part of the culture of City government over the long term.

Productivity Bank

The original Plan proposed the establishment of a Productivity Bank "to make loans for productivity initiatives to City departments, which the departments must repay over five years from operating budget savings." The Bank was established in 1992 with $20 million in funds from PICA's 1992 bond issue. The Bank increases the incentive for departments to save money and increase efficiency, by providing an institutionalized source of funding for projects that provide long-term improvements in the City's operational productivity, that cannot receive funding from the capital budget, and that are not easily funded within the constraints of the operating budget because their financial benefits are received over multiple years. Loans to departments are paid back with interest over five years from the time of the loan, from the budget of departments receiving the loans, so that the lending capability of the Bank will continue.

Through January 1995, the Bank has funded 11 projects for a total cost of $15.8 million, including a computerized collection system in the Revenue Department, a management information system to monitor the City's vehicle fleet, conversion of vehicles to natural gas, a computerized photo imaging system for the Police Department, personal computers and case management software for the Law Department, replacement of light bulbs in City offices with more energy-efficient bulbs, and automated document recording and mapping for the Records Department. To date, $3.7 million has been repaid to the Bank, and $3.9 million is budgeted to be repaid in FY95.

The original criterion for loans was that projects had to generate increased revenues or decreased costs over the five years from the time of the loan equal to twice the amount of the loan. This requirement has since been modified by the City so that the enhanced revenues or decreased expenditures resulting from the loan over the five years from the time of the loan must equal the amount needed to pay back the loan with interest. PICA Staff believes that this less restrictive criterion is appropriate only if it will allow more projects to be approved while still insuring that only projects with significant long-term operating benefits will be funded.

A new category of eligible projects has also been created recently by the City, which will allow Productivity Bank funding for projects that do not demonstrate clear reductions in cost or increases in revenues, but substantially and measurably improve service levels without increasing City costs. This expansion of the scope of projects that can be funded by the Bank is appropriate. However, PICA Staff is concerned about whether adequate systems are in place to monitor the service level impact of loan projects, to evaluate results and assist in making future investment decisions.

Initiatives

The Management and Productivity section of the original Plan included a long list of "potential" management and productivity initiatives which were not factored into Plan financial projections. Many of these initiatives have not been implemented; some are in the process of being implemented. These initiatives should be aggressively pursued to help preserve the City's long run financial stability. Examples of these initiatives include:

- Encouraging private companies and non-profit institutions to "adopt" portions of Fairmount Park to fund maintenance costs. This has not been implemented.

- Encourage more private fund raising efforts at the Free Library. This initiative is just getting underway, with a major fundraising campaign announced in April of 1995.

- Coordinate the efforts of OHCD, RDA, PHDC and PHA and, over time, consider a change in the laws in order to create a single housing agency for Philadelphia. While there has been some effort to coordinate homeless programs in the City, little progress appears to have been made to date in coordinating overall housing policy.

- Lease two of the five municipal cable television stations.

- Standard routes should be established for refuse collection to increase driver accountability, reduce the time spent in "warm-ups" and increase efficiency. This is in the process of implementation, with development of a computerized map and routing software, but delays in the communication system that will increase accountability are a source of PICA Staff concern.

- Long-term planning for equipment purchases should reflect the City's waste management goals. A zero-based analysis of fleet needs is still in the process of being developed. Plan projections of vehicle purchase costs still do not reflect long term planning for vehicle needs Citywide.

- Combine Gas and Water meter readings and collections and then possibly contract them out to PECO Energy.

- The section also contained a list of "potential asset sales" naming over 40 such assets. Most of the listed assets are still City property. Their sale should be pursued.

**Personnel**

Wages

The original Plan projected no salary increases for the life of the Plan. Actual increases were zero percent in FY93, zero percent in FY94, 2 percent in FY95 and 3 percent in FY96, higher than the Plan projection, but well below historical averages of previous years. With respect to salary restructuring, a major proposal of the original Plan, reducing starting salaries for Police officers and firefighters, was achieved.

The original Plan's proposal to totally eliminate longevity payments was not achieved. The Administration did succeed in delaying the start of longevity payments from 3 years after hiring to 5 years after hiring, for DC33 and DC47 employees, which according to the City results in $770,000 in annual savings. The current Plan suggests that a more modest change in longevity pay could occur, to freeze all employees at their current levels of longevity pay and eliminate longevity for future hires. This would result in savings of approximately $1.5 million, with savings increasing over time. Phasing out the longevity payments program would provide funds for instituting a more performance based compensation system.

Benefits

Significant savings have been achieved in the cost of employee benefits even though many of the measures proposed in the original Plan, such as requiring co-payments, eliminating retiree and school crossing guard benefits, consolidation of the City's five health care programs, and elimination of legal services benefits, were not implemented. Savings were achieved largely through one-time reductions in the City's monthly per employee contributions to union-administered health funds and a provision that future annual increases in these monthly contributions would equal the average rate of cost increase in the three largest Philadelphia HMOs. A low rate of cost increase has also been achieved in the City administered health plan, through increasing the percentage of employees enrolled in managed care programs, rebidding the City's dental and prescription plans, and streamlining the flex credits benefit. Significant structural changes were that the City would have the ability to appoint up to 20 percent of the board of trustees for the four union health funds, and that the union health funds would maintain financial records which the City trustees would have full access to, and that the City would have the right to select an independent CPA firm to audit the funds. Also provisions to insure non-duplication of benefits were instituted. Whether these provisions will be sufficient to allow continued modest growth in health benefits costs is unclear.

Overtime Savings

The original Plan projected savings in overtime costs through reductions in holidays and sick leave allowances. The Plan projected that the number of paid holidays would be reduced from 14 to 9, significantly reducing overtime costs in the Prisons, Police, Fire and

Streets Departments. Holidays were actually reduced to 10, close to but not quite the level of reduction projected in the original Plan. Holiday overtime has been reduced an estimated $7.2 million per year as a result. Further, in partial compensation for the reduction in holidays, personal days were increased from 3 to 4, which should result in increased regular overtime.

The Plan also projected that the number of annual sick days would be reduced from 20 to 10. The actual reduction achieved under new contracts is a reduction from 20 to 15 days for employees hired after October 1992 only. The high level of sick leave allowance is a major incentive to sick leave abuse. Problems also remain with weaknesses in City sick leave policy, which are described in the FY96-FY2000 Plan. The "Departmental Leave Usage Analysis," included in Quarterly City Managers Reports since the report for the first quarter of FY95, provides information on total leave usage and sick leave usage by City agency, which should assist in monitoring the results of sick leave policy and identifying problem areas. High use of sick leave, however, continues to be a factor driving up overtime costs.

The result of these initiatives can be seen in trends in overtime costs. Overtime costs have been reduced substantially from FY92 to FY94, with holiday overtime reduced from $20.3 million to $12.4 million, a reduction of $7.9 million (38.9 percent), and regular overtime reduced from $62.4 million to $59.6 million. According to the City, the reductions have been due to reductions in leave time, new work rules and schedules, and regular reporting and attention to overtime use. Further reductions are possible, however, since the City reports that a substantial amount of overtime cost is still the result of inefficient work practices that result from union contracts. The Quarterly City Managers Report now includes more detailed analyses of overtime utilization by City agency, which should assist in determining factors driving overtime costs and developing initiatives to reduce unnecessary overtime.

In its staff report on the original Plan, PICA Staff expressed concern that improved personnel complement control would be necessary to control overtime costs. The City has not relied on layoffs to achieve complement control, instead using contracting, redeployment of personnel displaced by contracting, attrition and hiring. PICA Staff is concerned whether these mechanisms have allowed desired levels to be achieved in all areas. In some areas, such as EMS, there has been some difficulty in achieving desired personnel levels, due to problems in recruiting.

Disability Reforms

The original Plan included initiatives to amend Civil Service Regulation 32 to limit its abuse by employees, reduce injury pay rates below regular pay rates to eliminate disincentives to return to work, revise the pension ordinance to eliminate "double-dipping," and realign the pension ordinance with Regulation 32 to mandate rehabilitation and redeployment of the partially disabled. Much of the original Plan's agenda with respect to disability system reform has been achieved or is in the process of being implemented. While disability costs continued to increase through FY94, the Plan projects reductions in disability costs beginning in FY95, and continuing through each year of the Plan. The savings over the long term are likely to be substantial, both for General Fund disability costs and pension costs, if the actions currently in the process of implementation are fully implemented.

**Debt**

The original Plan cited the problem of a high debt burden, with per capita debt at $2,892, and the problem of the statutory limit on tax-supported debt. The statutory debt limit is no longer an immediate problem due to PICA's role as a capital funding agency for the City over the past three years. During this time, maturing City debt has been retired, little additional City debt was issued, and PICA assisted in the early retirement of a substantial amount of high interest rate City debt. However, the problem of a high City debt burden remains in an economic if not a legal sense, since PICA debt service, as much as City debt service, reduces the level of discretionary resources available to the City.

Debt service as a percent of total General Fund revenues is estimated at 6.6 percent in FY95 and is projected to increase to 6.9 percent by FY2000. Combined PICA and City debt service as a percent of total PICA tax revenues and City General Fund revenues (less PICA City Account revenues) is estimated at 10.7 percent in FY95, and is projected to remain at approximately this level over the course of the FY96-FY2000 Plan. This high debt service burden reduces the City's flexibility to respond to budgetary shortfalls should they reemerge in the future. The FY96-FY2000 Plan does not propose any solutions to the high debt burden of the City.

A PICA Staff concern at the time of the original Plan was the need to develop internal guidelines for debt policy that would reflect the City's total revenues and total long-term obligations. The statutory debt limit in effect is an incomplete measure of the real debt capacity of the City since it relates only to one portion of the revenue generating capacity of the City, the real estate tax base, and one portion of the debt burden, the tax supported general obligation bonds of the City. The Plan states that the City will complete and implement an official debt policy during FY95. PICA Staff looks forward to reviewing this policy.

**Department of Human Services**

<u>Reduce Obligation Growth</u>

In the Department of Human Services (DHS), a major concern at the time of the original Plan was the rapid growth in obligations. Costs in the Children and Youth Division were increasing rapidly, driven primarily by increasing numbers of children in high cost institutional placements. Since then, cost growth has decelerated gradually, due to declining growth in total caseload and declining growth in high cost placements, and diversion of costs to Medicaid funding. Total DHS FY96 General Fund obligations are now projected to be $303.6 million or 8.0 percent lower than projected in the original Plan.

However, the Plan projects continued rapid DHS obligation growth. Revenue increases at the rate of the past several years are not likely. The Department must focus on further reducing obligation growth if net City cost growth is to be reduced to a level consistent with growth in the revenue base over the long term.

Maximize Title IV-E Funding

The original Plan included an initiative to increase Federal Title IV-E revenues through increasing the eligibility rate of children receiving DHS services. This initiative has been implemented successfully. The Department projects maintaining an eligibility rate of 81.4 percent for all children in placement for the full term of the FY96-FY2000 Plan, compared to a rate of 64 percent that was the original Plan target. Title IV-E revenues have increased rapidly in recent years, from $63.7 million in FY92 to $79.9 million in FY94 (including "retro" revenues that will be recognized in FY95), as a result of improved efforts to determine eligibility, and convincing providers to convert to non-profit status (since for-profit providers' services are not eligible for IV-E funding). The Plan projects a lower rate of increase in the FY96-FY2000 period, since no further increases in eligibility are assumed. The assumptions appear reasonable, since projections are based on calculations that relate projected IV-E revenue to projected obligations. However, a major concern of PICA Staff is the impact of possible welfare reform legislation on the Title IV-E program and other Federal child welfare programs that provide funding to DHS.

Achieve Appropriate Levels of State Funding Under Act 148

The original Plan and the current Plan are both based on the City's policy of funding mandated services only to the level of the certified needs-based budget. While DHS questions whether the amounts provided under the need based budget process established under Act 30 of 1991 were appropriate, it is important to note how rapidly combined State Act 148, Title IV-B and Title IV-A revenues have increased from FY90 to FY95. The increase has been primarily due to Act 30, which committed the State to a funding process based on "needs-based" budgets and a gradual increase of the State share of child welfare costs. Combined State Act 148 and Federal Title IV-B funding increased from $57.4 million in FY90 to $85.3 million in FY92 and $117.4 million in FY94, for an average annual increase of 19.6 percent from FY90 to FY94. Act 148 revenue is projected to drop to $111.6 million in FY95 because the FY95 State budget assumed implementation of a new federal funding source, Title IV-A, which is projected to bring $21.1 million in revenue to the City in FY95. If combined Act 148, Title IV-A and Title IV-B funding are received as projected in FY95, this would result in a increase of 13.0 percent from FY94 to FY95 for these three funding sources.

## Reduce the Social Worker to Caseload Ratio

Another original initiative was reducing the number of social workers per case for cases receiving contracted services, which has not been implemented due to the State's rejection of the proposal. In fact, DHS is actually proposing reducing the number of cases supervised by each social worker in its FY96 budget proposal to the State Department of Public Welfare (DPW). DHS is making a transition to providing fewer services directly and more services on a contract basis, including foster care and services to children in their own homes. A long term issue for DPW is whether it wishes to change its minimum staffing ratios when services are increasingly contracted out.

## Achieve Greater Medicaid Funding

The original Plan projected diverting costs to Medicaid funding under the Early and Periodic Screening, Diagnosis and Treatment (EPSDT) program, which was projected to increase revenue by $9 million each year from FY93 to FY96. While phase in of the diversion was delayed, actual impacts beginning in FY95 are projected to be higher. Actual FY94 costs diverted to Medicaid funding (which has a different Plan impact than increased revenue, since only a portion of all child welfare costs is City funded) were estimated at $7.7 million, and are projected at $14.7 million in FY95 and $16.2 million in FY96. In FY95, diversion is projected to be achieved for medical services to children in foster care, children receiving services in their own homes, children in residential treatment facilities receiving mental health services, and children in foster care who are HIV-positive. The Plan assumes that $1.5 million in costs for an additional category, pediatric nursing home services, will be diverted beginning in FY96. This diversion to Medicaid will have a positive short term impact on DHS costs, and may have a long term impact on growth rates if the diverted costs represent some of the faster growing components of DHS costs in recent years.

## Fundamental Changes in Service Delivery

The PICA Staff report on the original Plan noted that, in the long-run, improvements in the financial results of DHS cannot be achieved and maintained without fundamental change in the manner in which DHS provides services. The original Plan included three initiatives related to changes in service delivery. They were: to service 5 percent more out-of-home client days in home, and 5 percent more out-of-state client days in state, and concentrate on the prevention of problems. These initiatives were designed both to improve financial results and improve services.

The FY96-FY2000 Plan indicates that DHS has made progress in reducing the number of out of State placements, from 183 in July 1992 to 144 in July 1994. However, significant improvements have not appeared to date in the percentage of the caseload receiving in home and community based services, and the duration of out-of-home placement. The Department has implemented and is in the process of implementing several significant management reforms, which may assist in addressing the problems of duration of placement and excessive use of institutional services. However, these reforms have not had measurable impact to date. They are described below.

A computerized Family and Children Tracking System (FACTS) information system has been implemented which tracks all intake/investigation reports and child/youth placements, generates automatic billing, prints forms previously prepared by hand, and reminds staff when reports are due. As of February 1995, all child/youth placement tracking and billing functions were automated through the FACTS system. A key element needed to evaluate the effectiveness of various service types and improve management of DHS's caseload is better data, which the FACTS system should assist in providing.

The Children and Youth Division recently established a Quality Assurance Unit to review cases to maintain compliance with licensing requirements.

DHS is also in the process of developing a multidisciplinary review function to review children in high-cost, residential/institutional placements in order to assess the appropriateness of the services being provided. The rapid increase of high cost medical placements in recent years has been a major factor driving the overall increase in DHS obligations. Although no reported results have been achieved to date from this initiative, the initiative holds the potential of reducing cost or reducing the growth rate for costs of residential/institutional placements.

A new Centralized Resource Unit has been established with centralized responsibility for determining providers from whom services can be procured, based on availability of service, and on recommendations of social workers regarding appropriate service category. A statewide computer data base of provider agencies' available resources, PLANet, is used in locating available service slots. This is designed to allow social workers to concentrate on appropriate duties, and to avoid "overplacement" which can result when social workers will place children in a higher level of service than is needed because it is easier to find an available service slot.

**Department of Public Health (DPH)**

Reducing Non-Mandated Health Costs

An initiative included in the original Plan was reducing non-mandated health costs. The original Plan stated "efforts will be undertaken to establish and strengthen partnerships with local hospitals, academic medical centers, and the hospital community generally, in an attempt to assist uninsured patients with finding programs for which they are eligible. This will result in less demand at local health centers from the uninsured population--although no patients will be denied medical attention. In addition, DPH expects to be able to lower the cost to the City of non-mandated health services through productivity reforms and revenue enhancements."

This original Plan's approach to the reduction of non-mandated health costs has been largely abandoned. Instead, DPH has pursued a strategy of maximizing revenues at the Health Centers to reduce net costs rather than reducing costs through establishing stronger partnerships with private providers. Currently, the Department is focused on upgrading District Health Center services to position the Health Centers to compete in the managed care marketplace, to increase revenue from Medicaid patients who will in the future be covered under managed care. At the same time the Department expects that the Health Centers will continue to be a primary source of health care to the uninsured.

Despite the increase in revenues at the District Health Centers, and reductions in City net costs of the Philadelphia Nursing Home through competitive contracting since FY92, total Departmental unreimbursed obligations have remained at approximately the same level from FY92 to FY95. The current Plan projects no significant reduction in these costs through FY2000.

Much of the locally funded spending of the Health Department is for mandated services or represents a local investment that leverages a large amount of grant funding. Other spending, such as that for district health centers, could be reimbursed if Medicaid and other funding is aggressively pursued. PICA Staff remains concerned whether, given the large increase in grant funding in recent years, all local spending is really necessary, and an effective strategy to minimize net costs to the City within the public health goals of the City is being pursued.

Increase Medicaid Revenue Received at the District Health Centers

The original Plan projected increased District Health Center Medicaid revenue of over $7 million per year through improved classification and billing of costs, and certification of the District Health Centers as Federally Qualified Health Centers (FQHCs). The actual increase has been smaller, with Medicaid from the District Health Centers increasing from $1.8 million in FY92 to a projected $5.5 million in FY95. The increase has been due primarily to achievement of FQHC status and increased revenue from Medicaid recipients covered by HMOs. Staffing of State welfare officials in District Health Centers to make eligibility determinations ("outstationing") was a major focus of the original Plan, and has recently been implemented, but it appears to have had little impact. It is notable that the total increase in Medicaid revenue at the Health Centers has not kept pace with the increasing total costs of the Health Centers. The long term success of the City's efforts to increase Medicaid revenue at the District Health Centers will depend on the impact of the State Health Choices program, under which Medicaid services will be delivered through managed care networks.

Expanding EPSDT Funding

An initiative included in the original Plan was expanding EPSDT funding for a variety of services provided by the Department which had become eligible for funding under a recent expansion of the Medicaid program, such as immunization services provided in District Health Centers and environmental lead investigations. The Plan projected a revenue gain of over $800,000 annually, but Department does not currently report that any revenue gain has occurred. It appears that EPSDT is not separately reimbursed for managed care patients and for federally qualified health centers. There may still be a variety of services that DPH provides which are reimbursable under EPSDT, but no progress appears to have occurred on this.

Another part of the initiative was to divert Mental Health/Mental Retardation (MH/MR) costs to EPSDT funding. DPH reports that $2.1 million in annual MH/MR costs have been diverted to EPSDT funding. This is not necessarily a net savings to the City since a large percentage of MH/MR costs are reimbursed.

Reducing Net Costs of PNH

An initiative of the original Plan was reducing the net costs to the City of the operation of the Philadelphia Nursing Home (PNH), through increased Medicaid reimbursement based on a change in State reimbursement formulas, improved Medicaid billing for specialty services, and increased occupancy (which would result in a direct increase in revenue with a lesser increase in cost). This initiative was later abandoned and replaced by a plan to contract out operation of PNH. The original initiative projected enhanced revenues prior to discount of $2.1 million in FY93, $2.2 million in FY94, $2.3 million in FY95 and $2.4 million in FY96. Net costs of PNH were $6.7 million in FY90 and are projected to be reduced to $3.2 million in FY95 as a result of contracted operation, for an annual net savings to the City of $3.5 million in FY95. The Plan projects that this level of net costs of PNH will be maintained in future years. The savings from contract operation exceeds the original Plan projection of savings based only on revenue enhancement by $1.2 million in FY95, or over 50 percent.

Greater Incentives for Productivity at Health Centers

The original Plan proposed that the most productively managed District Health Centers (those with the greatest productivity gains and revenue enhancements) would receive favorable treatment such as increased administrative support, personnel and capital improvement spending. This idea was not implemented. However, this initiative has been replaced by another initiative designed to promote greater incentives for productivity at the Health Centers, which will create target expenditure and revenue budgets for individual Centers.

**Fire Department**

Lower Entry-level Salaries

The City's original Plan called for a $6,000 decrease in annual starting salaries for both Police and Fire Department uniformed personnel. The original Plan projected $6.5 million in savings after discounts over the life of the Plan from this initiative.

PICA Staff, in its report on the original Plan, expressed concern about this initiative because it was subject to the arbitration process. In November 1993, the arbitrator awarded the City the right to lower starting salaries of Fire uniformed personnel. The projected savings from this change have yet to be quantified by the City.

It should be noted, however, that other factors, such as mandated staffing levels, have caused Class 100 costs (salaries) to exceed original Plan projections, and continually exceed budgeted levels.

<u>Ladder Company Restaffing</u>

Though not discussed in the original Plan, the City pursued through the arbitration process a reduction in crew size for ladder trucks. The arbitration award did not allow the City to institute this initiative, resulting in significantly increased Class 100 costs.

The Department's overall class 100 costs were $1.5 million above projections in FY94 and are projected to be $800,000 over budget in FY95.

One of the factors contributing to Class 100 costs exceeding budgeted levels is the lack of holiday buy back. PICA Staff remains concerned about the continuing Class 100 budget overruns in the Fire Department.

<u>Emergency Medical Services Collections</u>

In the original Plan, the Department also had a revenue initiative to improve Emergency Medical Services (EMS) collections. The total revenue after discount over the life of the Plan was projected at $8.2 million.

The FY96-FY2000 Plan indicates that net EMS collections in FY94 were $5.5 million, an increase of $1.6 million over the FY92 level. The original Plan had projected a FY94 impact of $2.7 million from the EMS collections initiative before discount, and $2.0 million after discount. As a result, while EMS collections have improved, they still underperform the original Plan projections. The FY95 projection shows net EMS collections increasing to $6.2 million, which would bring results closer to Plan projected levels.

Even with the projected FY95 improvement, net EMS revenues are well below the City's cost of providing this service, and further efforts at revenue enhancement should be pursued, particularly in light of the increase in EMS costs likely to occur as a result of recent expansions in EMS staffing.

**Public Property**

Lease Savings

In the original Plan, the Department of Public Property had an initiative entitled Lease Savings. The Plan describes this expenditure decrease as emanating from a 10% reduction in leased office space. The original Plan projected savings of $3.2 million in FY94, $3.3 million in FY95, and $3.4 million in FY96 for total Plan savings of $10.5 million.

The City has yet to quantify accurately any savings from this initiative because of inadequate reporting practices within the Department of Public Property. PICA Staff urges the Department to comply with the Administration requests, and to submit accurate target spending plans on a timely basis.

Custodial Services

As another cost saving measure, the original Plan established an initiative to privatize a portion of custodial services. The City projected $733,000 in savings in FY93 growing to $812,690 in FY96. The City projected $3.1 million in savings for the life of this Plan.

Based on the most recent Quarterly City Managers Report, savings are on target for this initiative. Currently, the City has privatized custodial and maintenance services for both the Municipal Services Building and City Hall facilities, and has budgeted for private vendors to provide similar services at both the Curran-Fromhold Correctional Facility and the Criminal Justice Center upon completion of construction. PICA Staff is pleased with the City progress in this area especially because it begins to address our preventive maintenance concerns. PICA Staff remains concerned about the need for a comprehensive program to address ongoing preventative maintenance needs at all City facilities.

911 Users Fee

The original Plan included an initiative to establish a telephone user fee for 911 services, based on a State law under which the City was permitted to charge up to one dollar per line for these services. The fee is designed to recover capital and operating costs for the City's 911 communications system. A portion of the fee is allocated to the telephone company for the services.

As stated in previous PICA Staff reports, the City has successfully implemented this initiative. In the original Plan the City projected revenue collections of $5 million in FY93 growing to $7 million in FY96. The Quarterly City Managers Report indicates that this initiative generated $10.6 million in FY94, and is projecting $10.3 million in FY95 and FY96, exceeding original Plan projections by a significant margin.

**Streets Department**

Tip Fee Savings

In the original Plan, the Streets Department's largest initiative was the implementation of new waste disposal contracts which the City projected would produce $16.6 million in savings in FY95 and $18.5 million in FY96. The contracts would also enable the City to close two of its three transfer stations to produce savings of $2.6 million in FY94, $7.2 million in FY95, and $7.5 million in FY96.

In FY93, the City closed two transfer stations which the FY96-FY2000 Plan indicates reduced disposal costs by more than $15 per ton. Based on information provided in the two most recent Quarterly City Managers Reports it is unclear what financial impact this initiative has had on the General Fund. In the Quarterly Report for the fourth quarter of FY94, the Initiative Progress Report indicated savings to be 51% less than originally projected with "no explanation for difference from 5Yr. Plan". The progress of this initiative was not updated in the most recent Quarterly City Managers Report, so the current status of this initiative remains uncertain.

Discontinuation of Private Alley Lighting

In the original Plan, the City had hoped to discontinue private alley lighting. It was the City's contention that this would produce savings on electricity and maintenance costs associated with lighting private alley ways. The City originally projected savings in excess of $1 million beginning in FY93 with continued growth in the out years.

Based on pressure from City Council, the City has given up on this initiative. The FY96-FY2000 Plan indicates that beginning in late 1994 the City awarded a contract to begin the modernization on an estimated 18,000 alley lights throughout the City. This program is to be phased in over a three year period with a capital costs of $10.6 million.

Mechanical Brooms

In the 1992 Plan, the City anticipated purchasing mechanical brooms in order to reduce the number of blockmen employed by the City. The Plan indicated that total net saving from this initiative would be $4.2 million from FY93 to FY96.

This initiative has been a problem for the City since its inception. The first problem was an arbitration ruling in the union's favor that mandated reinstatement of sixteen employees by April 1995. Second, there were delays in the delivery of the first six vehicles. After finally receiving the mechanical brooms, the City experienced mechanical failure with the vehicles and had to temporarily discontinue their further use. The Quarterly City Managers Report indicates that projected savings from this initiative is down 55% in FY95.

## Fairmount Park Commission and Recreation Department

Savings Through Coordination

In the original Plan, the City anticipated eliminating duplicative maintenance tasks between the Fairmount Park Commission and the Recreation Department. Along with this initiative the City also anticipated combining the Recreation Department and Fairmount Park fleet to improve overall efficiency. In the original Plan, the City also indicated the need to reassign specific properties between the two operating departments.

This initiative has made virtually no progress over the last three fiscal years. In a recent meeting with the two departments, PICA Staff was told that the two were in the preliminary stages of discussing which properties to reassign and the possibility of using the same private contractors for lawn services. At no point in time did the Departments indicate when they would begin "positive" discussions on eliminating duplicative maintenance tasks. PICA Staff believes that the City cannot afford to neglect to address "hard issues" such as this which affect the efficiency of City operations. Achieving savings through greater interdepartmental coordination should be a major focus of City efforts.

## Law Department

Establish Recovery Unit

The original Plan included an initiative to establish a Recovery Unit to pursue all claims where City property has been damaged. No specific revenue amount was projected from this initiative. This unit has been established within the Risk Management Division of the Finance Department. Revenue was first generated in FY94, with $96,000 recovered in FY94. FY95 revenues are projected at $300,000.

Improve Claims Handling

The original Plan included an initiative to create a system for handling claims against the City. This initiative was designed to reduce indemnities costs to the City by systematically evaluating the merits of claims against the City and the City's exposure in such cases, and to improve the handling of the resolution of claims. Specific actions included were the creation of a professional claims analysis unit and more judicious use of outside law firms.

This initiative is in the process of implementation. A claims analysis unit has been established in the Risk Management Division of the Finance Department. Greater use of outside counsel has occurred, in part for reduction of the backlog of cases taking place under the Day Backward program. There has been a substantial increase in indemnities costs as the backlog of Day Backward cases has been reduced. In the long run, ongoing indemnities costs should be reduced if this initiative is successfully implemented.

Automate and Increase Staff in the Enforcement Division

The original Plan included an initiative to provide computers in the Enforcement Division of the Law Department, to improve the collection of delinquent taxes. Automation was projected to result in a one-time increase in tax collections spread over three years, equal to $10 million in FY94, $15 million in FY95, and $17 million in FY96, prior to discounts. Three other initiatives involved expanding staff in three separate revenue generating functions. 15 additional enforcement staff were to be added to increase enforcement of taxes and fines. This was projected to result in a revenue gain of $3 million in FY93 and increasing each year thereafter. 3 additional staff were to be added to process the backlog of sheriff sales to produce $300,000 in additional revenue in FY93, and increasing each year thereafter. 4 staff were to be hired to improve claims filing and collections of amounts due the City in all bankruptcy cases, resulting in additional revenue of $650,000 in FY93 and increasing each year thereafter. The additional staff were projected to result in additional costs of $400,000 annually beginning in FY93.

These initiatives were implemented. It is not possible to determine whether original Plan financial targets were achieved since the Law Department does not attempt to measure the impact of the additional automation or hiring in the Enforcement Division on collections. However, the initiative appears to have been successful on the basis of the large increase in “in-house” Law Department collections in FY93 and FY94 from the FY92 level. Total “in-house” Law Department collections increased significantly from $53.0 million in FY92 to $66.0 million in FY93. However, “in-house” collections declined in FY94 to $61.0 million and are projected to decline again in FY95. This reflects in part a decline in bankruptcy sale revenue, as well as the fact that the revenue increase due to the initiative is to some degree a one-time gain, as stated in the original Plan.

Consolidate Law Department Offices

The original plan projected that the five separate locations of the Department would be combined into one unit. Among the potential benefits of this initiative are the elimination of costs associated with having separate law libraries. Savings of $75,000 before discount were projected in FY95 and $77,625 in FY96. This initiative and its savings has not been achieved to date, and will apparently await the larger consolidation of Center City office space the City is now considering.

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## GENERAL FUND REVENUES

**Primary Areas of Concern**

- Impact of recession and economic restructuring on tax revenue growth rates
- Implementation hurdles needed to receive Riverboat Gambling Wagering Tax
- Plan assumption that revenue initiatives will continue to produce high levels of delinquent tax revenues
- Risks in estimating the impact of the Plan's proposed tax reduction and restructuring

**General Fund Revenue Projections FY95-FY2000 (millions)**

| Source | FY95 | Total FY96-FY2000 |
|---|---|---|
| Wage and Earnings Tax | $841.4 | $4,395.4 |
| Real Property Tax | 332.3 | 1,731.5 |
| Business Privilege Tax | 228.0 | 1,219.0 |
| Sales Tax | 86.0 | 477.3 |
| Real Prop. Transfer Tax | 50.0 | 265.4 |
| Riverboat Gambling Tax | 0.0 | 125.7 |
| Other Taxes | 58.3 | 320.2 |
| Total Taxes | 1,596.0 | 8,534.5 |
| Local Non-Tax | 155.6 | 794.1 |
| Other Governments | 390.1 | 2,206.9 |
| PICA City Account | 102.9 | 568.4 |
| Other Funds | 16.3 | 86.7 |
| Total | $2,260.9 | $12,190.6 |

### Introduction

The FY96-FY2000 Plan projections of total General Fund revenues appear reasonable. Projections of major components of revenues--taxes, locally generated non-tax revenues, revenues from other governments, PICA City Account revenues, and revenues from other funds--also appear reasonable.

The FY95 General Fund tax revenue projection on which the FY96-FY2000 Plan tax revenue projection is based appears reasonable and somewhat conservative. This is balanced out by projected growth rates that appear reasonable but slightly aggressive. The net result of the somewhat conservative FY95 "base" and slightly aggressive FY96-FY2000 growth rates is overall Plan tax revenue projections that appear reasonable.

A major risk with respect to the Plan tax revenue estimates is that a national recession during the Plan period could, at least temporarily, reduce growth rates significantly below Plan-projected levels. Also, the Plan assumes that delinquent tax collections will remain at current levels, which are very high compared to historical levels. Thus, the Plan is based on the assumption that revenue initiatives will continue to produce substantial delinquent tax revenue from better collection of delinquent taxes from currently registered tax payers and continued discovery of a significant number of previously unregistered taxpayers.

The Plan projects $125.7 million in revenue from a Riverboat Gambling Wagering Tax in the FY97-FY2000 period, which is highly speculative, due to implementation hurdles, such as passage of State legislation and a possible State or local referendum requirement, and questions about the level of tax revenue that would be generated. The risk that these revenues may not be received as projected is offset by the fact that the Plan assumes that the proposed tax reduction will not be instituted if riverboat gambling is not legalized, absent other improvements in City finances that would make it possible to institute the tax cut without riverboat gambling revenue. The impact of the projected Wage Tax cuts projected for FY97-FY2000 is approximately equal to the projected Plan revenues from Riverboat Gambling.

There are also PICA Staff concerns about the Plan's estimates of the impact of the proposed tax reduction and restructuring. Some significant assumptions were made in estimating the effect of the tax changes, particularly with respect to the Business Privilege Tax. Only time will tell if those assumptions were correct.

**FY96-FY2000 Projections of Total General Fund Revenues**

Total General Fund revenues are projected at $2,260.9 million in FY95, and are projected to increase 2.1 percent in FY96, 2.3 percent in FY97, 3.7 percent in FY98, 2.6 percent in FY99, and 2.3 percent in FY2000. Total revenues grow at rates below the Plan's assumed inflation rate of 3.5 percent in each year of the Plan except FY98. The average projected rate of increase over the FY95-FY2000 period is 2.6 percent, which is also below the Plan's assumed inflation rate.

**FY96-FY2000 Projections of General Fund Total Tax Revenues**

PICA Staff's analysis of the tax revenue projections in the FY96-FY2000 plan was separated into two parts. First, Staff analyzed the City's projections of tax revenue growth assuming no rate changes. Then, Staff analyzed the Plan projections of the impact of the proposed tax cuts in the Wage, Earnings and Net Profits taxes and the Business Privilege Tax on revenues. The discussion which follows next refers to the Plan's assumptions regarding tax growth assuming no statutory changes. A separate discussion subsequently follows which describes issues involved in estimating the impact of the proposed tax cuts.

Total General Fund tax revenues, assuming no statutory changes, are projected to increase 2.5 percent in FY96, 2.9 percent in FY97, and 3.0 percent in FY98-FY2000. In each year of the Plan, projected revenue growth is below the Plan-projected inflation rate of 3.5 percent. Growth rates for individual taxes are generally consistent with those used in the FY95-FY99 Plan. Growth rates for most taxes appear reasonable, but in some cases slightly aggressive.

Total General Fund tax revenues for FY95 are projected at $1,596.0 million, which appears reasonable and somewhat conservative based on reports of collections through March. Collections through March do not provide an indication as to likely full fiscal year results for the Real Estate Tax and the Business Privilege Tax, because the period when the majority of Business Privilege Taxes are collected has not yet arrived, and a substantial amount of Real Estate Taxes, which are collected primarily in the January through April period, have not yet been received. Through February, collections of Sales, Real Estate Transfer, and Parking taxes indicate that the Plan's FY95 projections for these tax revenue sources are on target. Through February, FY95 collections of the City portion of the Wage, Earnings and Net Profits taxes increased approximately 3.0 percent over the same period in FY94 (after making accounting adjustments), while the FY96-FY2000 Plan projects a 1.4 percent increase in FY95, suggesting that the Plan FY95 projection may be exceeded by $10 million. Collections of the PICA portion of the Wage, Earnings and Net Profits taxes similarly appear likely to exceed Plan projections, with collections through February increasing 6.0 percent over the same period in the prior fiscal year, while the Plan projects only a 1.6 percent growth. As a result of the strong performance to date in the Wage, Earnings and Net Profits taxes, overall Plan FY95 tax revenue estimates appear reasonable and slightly conservative.

The net result of the somewhat conservative FY95 revenue forecast and slightly aggressive growth rates is overall Plan tax revenue projections that appear reasonable.

**FY96-FY2000 Projections of Revenues from Individual Taxes**

*Real Property Tax*

Current Real Property Tax growth rates are projected at 0.7 percent in FY96, 1.7 percent in FY97, 1.5 percent in FY98, 1.7 percent in FY99, and 1.9 percent in FY2000. These rates are slightly lower than that contained in the FY95-FY99 plan, reflecting a slower than previously expected recovery in the real estate market. The projection is based on assumptions regarding the level of adjustments to assessments due to appeals, the level of new construction and the timing of its transfer to taxable property rolls under the tax abatement program, and growth in the assessment base due to growth in market values. These assumptions appear reasonable. The FY95 projection, the base from which Plan revenue projections are calculated, appears reasonable. Prior Real Estate taxes are projected to grow by 2.3 percent in FY96 and 3.9 percent in FY97, and remain flat in each of the years FY98-FY2000. Collections through March suggests that the FY95 projections may not be met, and will be significantly lower than in FY94. The City indicates that growth rates are projected to increase in FY96 and FY97 due to revenue initiatives. Nonetheless, this projection appears aggressive.

*Personal Property Tax*

Personal Property Taxes are projected to grow at 3.5 percent in each year of the FY96-FY2000 Plan. Collections of this tax are somewhat volatile due to fluctuations in the stock market, but the projected growth rate is below long term historical trends. The FY95 base upon which the growth is based appears reasonable, and the overall Plan projection appears reasonable.

*Wage and Earnings Tax*

The current (as opposed to delinquent) component of the City portion of Wage and Earnings Taxes is projected to increase 2.5 percent in FY96, 3.0 percent in FY97, and 3.5 percent in FY98-FY2000. The FY96-FY2000 Plan growth rates are approximately equal to the growth rates included in the FY95-FY99 Plan. These growth rates are based on the assumption that average wages per employee will increase by 3.0 percent in FY96, 3.5 percent in FY97, and 4.0 percent in FY98-FY2000, and that employment levels will decline by 0.5 percent in each year of the Plan. Projected growth rates appear reasonable, but slightly aggressive, particularly in the FY98-FY2000 period. The FY95 base from which these grow rates are projected appears reasonable, and may be somewhat conservative. The overall projection is reasonable, but PICA Staff has some concerns with regard to the Wage and Earnings Tax projection which are noted below.

Prior (delinquent) City Wage and Earnings Taxes are projected to increase at 2.5 percent in FY96, 1.1 percent in FY97, 2.5 percent in FY98, 1.9 percent in FY99 and 2.2 percent in FY2000. While these growth rates are below the rates projected for the current portion of these taxes, they would require sustaining a relatively high level of prior collections as a percent of current collections in historical terms, and appear somewhat aggressive as a result. The projection assumes continued success with respect to revenue initiatives such as Revenue Department computerized collections and Law Department collections.

*Business Privilege Tax*

Current Business Privilege Taxes (BPT) are projected to increase by 4.0 percent each year in FY96-FY98, and 4.5 percent each year in FY99-FY2000. These rates are consistent with the prior Plan, for every year except FY98, in which the prior Plan had projected 4.5 percent growth. The volatility of this tax makes it more difficult to project, but projected growth is below long-term historical averages. The FY95 base from which growth is projected appears reasonable since it shows a 3.5 percent increase over the FY94 level, although collections to date provide little indication as to whether the FY95 projection is likely to be achieved, since most collections from this tax are received in the final quarter of the fiscal year. The projection of current BPT revenues appears reasonable. Prior Business Privilege Taxes are projected to increase 5.1 percent in FY96, 5.1 percent in FY97, zero percent in FY98, 1.0 percent in FY99 and zero percent in FY2000. As in the case of prior Real Property and Wage and Earnings Taxes, PICA Staff believes this projection is somewhat aggressive due to its assuming a continued high level of prior collections as a percent of current collections. Continued success with regard to revenue initiatives will be needed to meet this projection.

*Net Profits Tax*

The City portion of the Net Profits Tax is projected to remain flat at the FY95 level through FY2000. This is clearly a conservative assumption, as there is no reason to expect this portion of the tax base would not perform as well as the Wage and Earnings Tax.

*Sales Tax*

The Sales Tax is projected to increase at 3.5 percent in each year of the Plan, which is higher than projected current Wage and Earnings Tax growth of 2.5 percent in FY96 and 3.0 percent in FY97, and equals projected current Wage and Earnings Tax growth in FY98-FY2000. Shopping habits of City residents and workers, and the impact of the hospitality and tourism sectors on City retail sales will be key factors driving this tax. An assumption of 3.5 percent growth is reasonable. The FY95 base projection also appears reasonable.

*Amusement Tax*

The Amusement Tax is projected to grow 12.7 percent in FY96, 3.4 percent in FY97, and 3.5 percent in FY98-FY2000. The large growth rate in FY96 reflects the depressed collection level of FY95 due to baseball and hockey strikes. The projection appears reasonable.

*Real Property Transfer Tax*

The Real Property Transfer Tax is projected to grow by 2.0 percent in each year of the Plan. This below-inflation rate growth is based on the fact that the projected FY95 base is believed by the City to be unusually high due to the impact of interest rates on housing sales in FY95. Based on collection experience to date, PICA Staff believes the FY95 base is likely too high. However, the low projected growth rate in all five years of the Plan results in an overall projection that appears reasonable.

*Riverboat Gambling Wagering Tax*

Revenues from this new revenue source are projected beginning in FY97 at $17.5 million, based on half year implementation, and increasing to $35.0 million in FY98. Revenues are projected to increase 3.0 percent in FY99 and FY2000. PICA Staff has concerns about inclusion of this speculative revenue source in the Plan revenue estimate. These concerns are described in a separate discussion below.

*Parking Tax*

The Parking Tax is projected to increase by 3.5 percent in each year of the Plan. Both the growth rates and the FY95 base projection appear reasonable. The impact of a recent initiative to improve enforcement of the Parking Tax has not been factored into the projections. Success with that initiative may further increase collections.

**FY96-FY2000 Projections of Non-Tax Revenues**

Plan estimates of General Fund Locally Generated Non-Tax Revenues appear reasonable. Significant assumptions were made with respect to revenues from Payments in Lieu of Taxes (PILOTs), additional revenues from fee increases, revenues received from the Philadelphia Parking Authority, and interest earnings. Total Locally Generated Non-Tax Revenues are projected at $155.6 million in FY95, and are projected to decline 0.7 percent in FY96, and increase by 0.3 percent in FY97, 3.4 percent in FY98, 0.9 percent in FY99, and 0.7 percent in FY2000.

Plan estimates of General Fund Revenue from Other Governments also appear reasonable. Key assumptions include PGW revenues of $18 million annually; receiving approximately $4 million in annual Southeastern Pennsylvania Transportation Authority (SEPTA) debt service reimbursement; and increases in County Health Act revenues, District Health Center Medicaid revenues, State Act 205 pension aid, and Utility Tax refund revenues. There are also a number of issues relating to DHS revenues which are discussed in the "Major Areas of PICA Staff Concern" section of this report. Total revenue from other governments is projected at $390.1 million in FY95, and is projected to increase 7.4 percent in FY96, to decline 0.7 percent in FY97, and increase 4.9 percent in FY98, 4.8 percent in FY99, and 4.8 percent in FY2000.

PICA City Account revenue estimates appear reasonable. PICA City Account revenues are estimated based on projected PICA Tax revenues, PICA debt service, and an estimate of $6.0 million in PICA annual interest income on reserve funds additionally remitted to the City. PICA City Account revenue is projected at $102.9 million in FY95, and is projected to decline 3.0 percent in FY96, and increase 6.0 percent in FY97, 6.9 percent in FY98, 6.6 percent in FY99, and 6.4 percent in FY2000.

Plan estimates of Revenues from Other Funds also appear reasonable. These revenues are primarily made up of payments from the Water and Aviation Fund for services performed and costs borne by the General Fund, the Water Fund "scoop" payment, and an Aviation Fund payment in lieu of taxes. These revenues are projected at $16.3 million in FY95, and are projected to increase 2.9 percent in FY96, and 1.5 percent in each year from FY97 to FY2000.

## Major Areas of PICA Staff Concern

**Projected Tax Revenue Growth Rates --** ***A cyclical downturn during the Plan period, and the impact of ongoing restructuring in the City's industrial composition, could result in lower revenue growth than projected***

A PICA Staff concern relating to Plan revenue growth rates is the impact a national recession would have on the City. The sensitivity of the City's tax base to cyclical changes in economic growth rates is evident from a review of City tax revenues over the past decade adjusted for changes in tax laws. While the City is currently on an upswing in the cycle, the high degree of cyclical sensitivity of General Fund revenues suggests the possibility that significantly lower growth rates could return in the event of a national recession. The FY96-FY2000 Plan projects General Fund tax revenue will grow at approximately 3.0 percent in the FY96-FY2000 period, which is approximately the rate of growth projected for FY95. However, nationally, 1994 was a period of rapid economic growth which is very unlikely to be sustained, on average, over the next five years. PICA Staff's concern is that the City's economic performance relative to the nation will have to improve for the City to maintain the FY95 rate of tax base growth over all five years of the Plan.

With respect to the projection of Wage and Earnings taxes, a major concern is that employment growth in the City continues to lag national employment growth. The Plan's assumption of employment loss of 0.5 percent per year is conservative in relation to recent trends. However, a significant slowdown in national employment growth could make this projection hard to meet if City employment growth does not improve relative to national trends. Another concern is the projection of increasing wage growth in the out-years of the Plan. Earnings per job growth in recent years has been below historical averages, and available data do not suggest that wage growth is increasing. Further, PICA Staff remains concerned about potential weakness in some of the industrial sectors that have been major contributors to earnings growth in the City over the past decade, including finance, insurance, real estate, health, legal, education and social services.

**Riverboat Gambling Wagering Tax --** ***Major obstacles to implementation need to be overcome to realize this revenue source at Plan-projected levels***

Another significant concern is the inclusion of revenues from the Riverboat Gambling Wagering Tax beginning in FY97. At this point, such a revenue source is speculative, given the obstacles to implementation that exist. These obstacles include the need for passage of State legislation, the possible need for approval in an statewide and/or local referenda, and the need for infrastructure improvements along the river. Assuming riverboat gambling is eventually implemented, PICA Staff is also concerned with the timing of such implementation and that the timing and level of revenue receipts will be consistent with Plan projections. The Plan projects revenues of $17.5 million in FY97 from this source, increasing to $35.0 million in FY98, $36.1 million in FY99 and $37.1 million in FY2000.

PICA Staff accepts the inclusion of this speculative revenue source in the Plan because the City has stated that the proposed tax reductions will not be instituted if riverboat gambling is not legalized, and Plan balance cannot be maintained without foregoing the proposed tax reductions. Given the importance of the tax cut to the future of the City's economy, as stated in the Plan, it is a concern that the Plan balance is yet so delicate that the projected tax cut can only be included in the Plan by assuming additional speculative revenues. This underlines the importance of continued pursuit of management and productivity improvements to allow for continued improvement in service levels and reductions in cost, to assure that Plan balance can be maintained while preserving the City's ability to deliver its promised tax cuts.

**Delinquent Taxes -- *The Plan assumes that current levels of collections of delinquent taxes, that are high in relation to historical levels, will be maintained, which will require continued impact of revenue initiatives***

Another concern with regard to tax revenue projections is the projection for overall revenues from delinquent taxes. Revenues from delinquent taxes for five major taxes (Real Property, Personal Property, Wage, Earnings, Net Profits and Mercantile License/Business Privilege) have increased substantially since FY84 both as a percent of total collections and in absolute terms. For these five taxes, revenues from delinquents have increased from $29.7 million in FY84 to $91.4 million in FY94, an average annual increase of 11.9 percent. Revenues from delinquent taxes were 2.9 percent of total revenues in FY84, and increased to 6.5 percent of total revenues in FY94. The FY96-FY2000 Plan projects that delinquent collections from these tax sources will hold at approximately 6.5 percent of total revenues for the FY96-FY2000 period, increasing to $100.3 million by FY2000. Maintaining this fairly high level of delinquent collections will require continued success in implementing revenue initiatives.

The Plan projection is based on a projection of FY95 prior revenues from these five sources of $91.5 million, essentially holding at the FY94 actual level of $91.4 million. However, FY95 collections through February of prior taxes for these five taxes are $44.4 million, compared to $47.6 million in the same period in FY94, suggesting the FY95 projection is unlikely to be met. Further, Law Department collections declined from $72.0 million in FY93 to $70.3 million in FY94 and are projected to decline again to $68 million in FY95. To some extent this decline may be a short term effect, as the Law Department has stated that its collections were artificially inflated in FY93 due to an unusually large amount of bankruptcy revenue, and that referrals of delinquent tax cases from the Revenue Department to the Law Department have declined in FY95 due to the transition to new computer systems in the Revenue Department. Although these effects may be short term, the lower collection experience to date still raises a concern about whether Plan projections of delinquent revenues will be met.

**Proposed Tax Reduction and Restructuring --** ***There are some risks involved in estimating the impact of the proposed changes in the tax structure, particularly with respect to the Business Privilege Tax***

The Plan makes some key assumptions regarding the impact of the proposed tax reduction and restructuring for the Wage, Earnings, and Net Profits Taxes and the Business Privilege Tax. The Plan assumes that the impact of the Wage, Earnings and Net Profits Tax cut proposal on City revenues is $10.6 million in lost revenue in FY96, increasing to $81.9 million in FY2000, for a total FY96-FY2000 Plan impact of $211.5 million in lost revenue. The Plan does not assume that the tax cut proposal will result in increased growth in the base of the taxes, so the calculation of the impact of the tax cut on current Wage, Earnings and Net Profits Tax collections is straightforward. However, some assumptions have to be made with regard to the impact on prior collections, and the Plan's assumptions in this regard appear aggressive, although the impact on Plan revenues is not significant.

The Plan estimates that the reduction and restructuring of the Business Privilege Tax will result in a reduction in revenues of $7.4 million in FY96, increasing to $20.0 million in FY2000, for a total FY96-FY2000 revenue reduction of $63.5 million. The estimate of this impact does not assume any increase in the growth of the tax base resulting from the tax change. As in the case of the Plan estimate of the impact of cuts in the Wage, Earnings and Net Profits taxes, PICA Staff is concerned that City estimates of the impact of the BPT tax cut did not assume any reduction in prior BPT taxes over the life of the Plan.

In addition, there is some risk to the Plan resulting from significant assumptions made in estimating the impact of the proposed changes in the Business Privilege Tax. Under the proposal, tax rates will be reduced by the same percentages in each year of the Plan for the regular gross receipts tax as well as the alternative tax rates that manufacturers, wholesalers and retailers can elect to pay. The assumption made is that the proportion of the total BPT tax base attributed to the gross receipts tax will remain at approximately 45 percent, the FY93 level. This may change significantly as a result of changes in profitability over the Plan period.

The Plan also estimates that the proposed double-weighting of gross receipts will result in an annual loss of $700,000. Generally, companies with substantial physical presence in the City will pay less under this change, and companies without a substantial presence will pay more. Based on data from sample of BPT taxpayers with a wide range of apportionment levels, the City estimates that revenues will increase by approximately $7.9 million from companies paying more under the proposal and revenues will decrease by approximately $8.6 million for companies paying less, for a net annual reduction of $700,000 in BPT revenues. While the method of estimation appears sound, the actual impact may vary somewhat. While the change is likely to have a positive impact on firms located in the City, with attendant positive impacts on City employment and non-BPT General Fund revenues, the net impact on BPT revenues is subject to substantial uncertainty.

The Plan projection of BPT revenue also assumes an increase of $200,000 annually from changing the interest rate paid on delinquent BPT payments to conform with the State rate.

## OBLIGATIONS OF PRINCIPAL OPERATING DEPARTMENTS

### Department of Public Health (DPH)

DPH obligations are projected at $120.9 million in FY96, which is $8.9 million (7.9 percent) greater than the current FY95 projection. The major component of the increase is Class 200 (purchase of services) obligations, which are projected to increase $8.4 million or 11.8 percent, due to a $2.5 million (18.2 percent) increase in the cost of the contract for prison health services, combined with a $5.2 million (18.1 percent) increase in Philadelphia Nursing Home (PNH) Class 200 obligations, due to the impact of an increased census at PNH on pass-through health insurance reimbursements. The cost of the contract for prison health services is projected to increase due to an increased level of services provided under the contract.

Under the FY96-FY2000 Plan, out-year growth uses the standard Plan assumptions. For Class 100 (employee compensation), growth in FY97 is 2.3 percent, reflecting the impact of annualizing the 3 percent wage increase that will be received on April 1, 1996 under the current labor contract. No additional growth is projected in FY98-FY2000. For Class 200 and 300/400 (materials and supplies/equipment) obligations, 1.5 percent growth is projected in each of the Plan outyears, from FY97 to FY2000. An additional assumption is that Class 800 (payments to other funds) obligations will remain constant at $1.5 million each year from FY96 to FY2000. Class 800 obligations reflect pass-through reimbursements for PNH capital costs.

The result of these assumptions is FY2000 obligations of $126.7 million, an average annual increase of 1.2 percent over the FY96 projected level.

Total departmental revenues are projected at $52.3 million in FY96, an increase of $5.5 million or 11.7 percent over the FY95 level, due primarily to an increase of $5.0 million in Medicaid pass-through revenue to PNH, the result of a projected increase in the average census at the facility. Total revenues are projected to increase to $58.1 million in FY2000, for an average annual increase of 2.6 percent over the FY96-FY2000 period. The increases are primarily due to increases in Medicaid pass-through revenue for PNH and increasing Medicaid revenue for the District Health Centers.

Unreimbursed obligations are projected at $68.6 million in FY96, and increase of $3.4 million (5.2 percent) over the FY95 level. Unreimbursed obligations are projected to remain constant at $68.6 million over each of the five years of the Plan.

### Department of Human Services (DHS)

The original draft of the Plan was changed prior to its submission to PICA, to transfer $20.0 million of DHS departmental revenues and obligations from the General Fund to the Grants Revenue Fund in each of the final four years of the Plan, FY97-FY2000. This change was made to address PICA Staff concerns about the achievability of total Federal revenues (primarily Title IV-E and Title IV-A) projections contained in the original Plan, given the uncertainty about the achievability of Title IV-A revenues and the potential impact of proposed Federal welfare reforms. The discussion below refers to projected General Fund obligations and revenues including the $20 million annually in obligations and revenues transferred into the Grants Fund.

DHS obligations are projected at $303.6 million in FY96, an increase of $24.7 million (8.9 percent) over the projected FY95 level. The major source of the increase is a Class 200 increase of $21.3 million (9.3 percent), due primarily to a $4.9 million (3.1 percent) increase in the cost of purchased placement services, a $7.7 million (73.3 percent) increase in the cost of purchased services to children in their own homes (SCOH), and a $6.7 million increase due to “initiatives” which have been proposed by DHS to the State Department of Public Welfare (DPW) as efforts to expand and improve services. The initiatives include $4.3 million for higher foster care rates as part of an effort to standardize foster care service standards and rates among southeastern Pennsylvania counties, and $1.1 million to increase rates for group homes to increase availability of the service to enable reductions in more expensive placements. The increase in the cost of purchased services for services to children in their own homes is due to a departmental initiative to provide purchased SCOH services to children that currently receive direct services. This is designed to improve the quality of services provided to this population and prevent more cases from entering more expensive placement services.

For the FY96-FY2000 Plan, Class 100 costs increase 6.1 percent in FY97, while all other major departments increase 2.3 percent or less (2.3 percent is the level of increase attributable to the annualization of the 3 percent wage increase beginning April 1, 1996 under the current labor contract). Class 100 costs increase 1.6 percent in FY98, 1.4 percent in FY99, and 2.0 percent in FY2000, while all other major departments have increases of zero in these years (except for Streets (Other than Sanitation), which increases 1.7 percent in FY98). These increases are projected to provide for increased staffing needs for decentralized offices, Family Centers, and to increase social worker to case ratios in FY96 and maintain them in later years. Class 200 costs increase 5.7 percent in FY97, 7.0 percent in FY98, 6.7 percent in FY99 and 6.7 percent in FY2000. By contrast, Class 200 costs in all other major departments increase at or near the standard assumption of 1.5 percent growth (except for First Judicial District, which increases at zero percent under the zero-growth budget agreement). The significantly higher growth rates projected in DHS reflect rapid growth in adoption subsidies, SCOH, Day Care, and medical-MH/MR, and modest growth in foster family care. These growth rates are significantly higher than those which were projected in the FY95-FY99 Plan. Due to the deceleration in growth rates in recent months, actual growth is likely to be slower than projected.

Departmental revenues are projected at $250.0 million in FY96, an increase of $19.9 million (8.6 percent), due to increases in Act 148 revenue of $11.3 million, $12.8 million in Title IV-A revenue, and $6.1 million in Title IV-E revenue. FY2000 revenues are projected at $319.1 million, for an average annual increase of 6.3 percent over the life of the Plan. The increases in projected IV-E revenue are consistent with projected obligations, and reflect historical trends in the proportion of children receiving placement services that are eligible for IV-E and a projected constant Federal financial participation rate. Projected IV-A revenue is more speculative at this time due to the lack of a track record in receiving IV-A revenue. It appears that the projected IV-A revenues are somewhat aggressive since the projected growth rates exceed projected overall DHS obligation growth rates. However, DHS maintains that this is because the estimate for the first year of IV-A revenue is conservative in relation to its estimate of what DHS is eligible to receive under the approved State plan for IV-A. Additional IV-A collection experience should enable a more reliable projection of this revenue source in future years.

Projected Act 148 revenue (which includes some Federal revenue from Title IV-B which is allocated along with State appropriation funds) normally should grow at the rate of total departmental obligations, after subtracting other revenues from other sources. This reflects the methodology of reimbursement under Act 148 and Act 30, which provide that total DHS obligations are first reduced by the amount of Federal and other reimbursements, and that the remaining unreimbursed obligations receive funding (using State appropriations and Title IV-B funds) at rates between 50 percent to 100 percent, depending on the type of service. Assuming no significant change in the distribution of services provided by DHS, Act 148 revenues should grow at the rate of obligations less revenue sources other than Act 148. Under the Plan, Act 148 projections grow at an average annual rate of 6.3 percent from FY95 to FY2000, while obligations less all revenues other than Act 148 grow at 4.6 percent. This disparity is the source of some concern to PICA Staff. However, it appears justifiable due to the projected increase in the proportion of the departments services made up of SCOH and community based placements, and the decrease in the proportion of services made up of institutional placements, since SCOH and community based placement services are reimbursed at higher rates.

Total DHS unreimbursed obligations are projected at $53.6 million in FY96, an increase of $4.8 million (9.9 percent) from the FY95 level. Unreimbursed obligations are projected to increase to $60.4 million in FY2000, an average annual increase of 3.0 percent.

**Fire Department**

Fire Department expenditures are projected to total $120.8 million in FY96 which is $3.2 million or 2.6% more than projected for FY95. The major component of the Department’s projected increase is in Class 100 expenditures which are estimated to grow 2.9% in FY96 and another 1.5% ($1.6 million) in FY97. The remaining out-years show zero percent growth in Class 100 spending.

Fire Department expenditures are projected to total $123.2 million in FY2000 which is $5.6 million or 4% over FY95 cost projections. The major factor for this increase in addition to Class 100 spending is a flat 1.5% increase in all other expenditures each year throughout the life of the Plan.

In the City's most recent Quarterly Managers Report dated February 15, 1995 current projections indicate that Class 100 expenditures are projected to be $2.9 million over budget. The City's transfer ordinance indicates that this increase is a result of water rate changes, the Administration's decision to increase EMS services in the spring of FY95, and finally because the Department did not fully anticipate the cost impact of the 1993 contract arbitration award.

**Fleet Management**

FY96 Office of Fleet Management (OFM) obligations (excluding vehicle acquisition) are $530,000 or 1.4% more than projected FY95. The major reason for this increase is projected increases in Class 100 (salaries) and Class 300 (purchase of parts and supplies) spending. Class 100 is expected to grow 2.2% in FY96 and 2.26% in FY97 with zero percent growth in the out-years. All other Department costs generally increase between 1.45 and 1.5% throughout the life of the Plan.

OFM projected vehicle acquisition expenditures (Class 400) total $84.1 million dollars throughout the life of the Plan. FY96 vehicle acquisition expenditures total $16.5 million growing to $20.4 million in FY2000. The Department has indicated that there is no detailed underlying analysis to substantiate these projections.

Currently, obligations are $828,682 over original OFM projections. This is because FY95 automotive parts purchases were higher than expected. A mid-year transfer ordinance reappropriated funds to cover these costs. Class 100 spending is currently slightly below original projections.

**Police Department**

FY96 Police Department obligations total $10.21 million or 3.25% more than the FY95 obligations in the Plan. The major component of the Department's increase in costs is Class 100 expenditures which grow by $9.06 million or 3.1%. The major reason for the increases in FY96 are increases in longevity and promotion payments as well as a 3% across-the-board salary increase which takes effect January 1, 1996. In FY96 the Department also anticipates expanding civilian hiring by adding an additional 72 communication dispatchers. This will cost the Department approximately an additional $1.2 million in FY96.

The Police Department anticipated establishing a new helicopter unit in FY96. The City originally anticipated full capital funding from the State with a Class 200 operating cost of $1.1 million to the Department. When questioned the City was unable to identify specifics of how these funds would be spent.

Since the publication of the Plan, the State, for the second consecutive year, has removed from its budget the capital funds allotted for the City helicopter unit. In a recent PICA Staff meeting with the Police Commissioner, PICA Staff was advised that, unless additional capital funds are found, this unit will not come into operation in FY96.

In order to further improve public safety throughout the City, the Administration contemplates adding 753 uniformed officers to the Police Department. These officers will be partially funded with proceeds from the Federal Crime Bill over the next three fiscal years. Based on information provided to PICA, the additional officers are being employed as follows: 153 - January 1, 1995, 200 - January 1, 1996, 200 - July 1, 1996, and 200 - July 1, 1997. The Administration has committed to continuing to staff these positions after Federal funding has been terminated.

**Department of Public Property**

The Department of Public Property's FY96 obligations increase $5.94 million over FY95 projected totals. The major components that increase obligations are Class 100 (salaries) which increases 2.2% and Class 200 (purchase of services) part of which represents a new custodial contract for the Curran Fromhold Correctional Facility.

Vehicle leasing costs are projected to decrease and eventually phase out over the life of the Plan. Utility costs are projected to be relatively flat, and Space Rental costs decrease 3% in FY96 and 3.1% in FY97. Space costs remain relatively flat in the out-years of the Plan.

The Quarterly Managers Reports indicate that Public Property's Class 100 costs are projected to equate to amounts budgeted in FY95. Utility costs are projected to be $3.5 million below original projections because of the relatively warm winter and because of telecommunication savings. SEPTA's subsidy payment for debt service is projected to be $4.6 million over original projections. A mid-year transfer ordinance was passed by City Council to correct this revenue/expenditure matter, which will have no negative impact of FY95's fund balance.

**Streets Department**

The Plan projects that the Department's FY96 obligations will remain relatively flat from FY95. Total obligations increase only $640,000 or .5%. The only major component that increases is Class 100 spending (personnel costs). This is due to a 3% across the board salary increase in January 1996.

Based on the most recent Quarterly Managers Report FY95 obligations are projected to be slightly under budget. It should be noted however that overtime costs are projected to be $1.1 million over budget. When questioned by PICA Staff, the Department was unable to provide a specific reason for the overage.

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## MAJOR AREAS OF PICA STAFF CONCERN

Department of Human Services (DHS)

**State Funding of DHS-Proposed Initiatives --** ***The Plan assumes State funding under Act 148 and Act 30 of some significant changes in service delivery, which the State may or may not approve for funding***

The Department's "needs based budget" proposal for FY96 proposes State Act 148 funding for initiatives for service expansion or reform and several projects that were previously funded by special grants. The Plan assumes State approval of at least some of these initiatives and "grant pick-ups". Without State approval of these items, meeting Plan projections of net DHS costs will require DHS to not implement some of these initiatives and cut off funding for some currently grant funded programs.

These initiatives include: housing social workers in decentralized offices throughout the City rather than one centralized Center City location; expanding the number of "Family Centers" where various health and social services would be provided to prevent child abuse and neglect; providing purchased Services to Children in their Home (SCOH) to children who are currently receiving SCOH program services directly from DHS social workers; increasing rates for SCOH to expand availability of services; increased rates for Foster Care to standardize service levels with the suburban counties; new staff to assess service needs of juveniles to reduce their length of stay in the Youth Study Center; parent education; and increased rates for group homes to increase the availability of service and reduce utilization of more expensive placement services. Plan obligation projections include additional costs related to many of these initiatives, but State approval to fund the initiatives as part of ongoing Act 148 funding has not yet been received.

If the State decides not to fund these initiatives, an increase in unreimbursed obligations could result if DHS chooses to pursue the initiatives without State funding. While the Department has indicated to PICA Staff that it will not pursue these initiatives if they result in an increase in net costs to the City, PICA Staff is concerned about this issue since many of the programs proposed are preventative and could reduce net costs in the long run.

**Impact of Medicaid Managed Care --** ***A major source of the reduced growth rate for DHS obligations in recent years has been expanded coverage of child medical services under Medicaid, and diversion of funding responsibility to that program, but it is unclear how the proposed conversion of the Medicaid program to a managed care basis would affect reimbursements to DHS providers, and (indirectly) DHS costs***

Beginning in FY94, DHS has been successful in diverting the costs of certain medical services for children receiving contracted services to Medicaid funding. The amount of DHS costs diverted to Medicaid was estimated at \$7.7 million in FY94, and is projected to increase to \$14.7 million in FY95 and \$16.2 million in FY96. Under the State Health Choices program, Medicaid services will be delivered through managed care networks. To what extent current DHS providers will be qualified to receive Medicaid funding under Health Choices, and what would be the impact of Health Choices on reimbursements to providers, is uncertain. The impact of Health Choices on reimbursements received by providers could result in pressure for DHS to make up any difference through additional funding, thus indirectly affecting DHS costs. In addition, in cases where current DHS service providers do not become part of approved managed care networks under Health Choices, DHS may have to utilize new service providers that are part of such networks, disrupting the continuity of care with significant impacts on DHS's current caseload.

**Implementation of Act 30 --** ***The State's interpretation of Act 30 could have an adverse impact on City unreimbursed obligations, and the continuing disagreements between the City and State regarding the proper interpretation of Act 30 raise questions about the City's ability to accurately project Act 148 revenue in the Plan***

In the FY96-FY2000 Plan, the City asserts that there are deviations between the State funding process and the spirit of Act 30 and the settlement agreement between the State and the counties which led to the legislation, which set up a "needs-based" funding process for county children and youth programs statewide. In applying criteria for accepted salary costs that do not reflect differences in labor markets across the State and in applying fixed caps on allowable year to year increases, according to the City, the State has not recognized real differences in the cost of providing mandated services in different counties, which are driven by labor market trends and trends in the number of children receiving services. PICA Staff is concerned that the State's interpretation of Act 30 could result in an adverse impact on City unreimbursed obligations. Also, PICA Staff is concerned about the ability of the City to accurately predict funding levels in the Plan, given the fact that disagreement continues to exist about appropriate funding levels under Act 30.

**DHS Federal Revenues --** ***The potential for Federal welfare reforms and the early stages of implementation of Title IV-A funding raise concerns about whether total Federal revenue received by DHS will meet Plan projections***

A major source of DHS departmental revenue, Federal Title IV-A Emergency Assistance revenue, is a new source of General Fund revenue without a track record that can enable reliable revenue projections. Even assuming the program is not changed significantly as a result of Federal welfare reform, there is a concern whether funding will be received as currently projected, given the lack of a track record to ascertain the level of DHS spending that is reimbursable under Federal regulations. Further, there is strong likelihood that this program and all Federal child welfare programs will be changed significantly as a result of Federal welfare reforms. The impact of such changes on the types of programs that the Federal government will fund, and the overall levels of Federal funding, is uncertain. However, the rapid rate of increase in total Federal funding (including IV-E and IV-A funds) in the Plan raises a concern about whether Plan-projected total Federal revenue levels will be achieved. In addition, under Federal welfare reforms, Federal funding may no longer be distributed directly to the City as an entitlement, but may instead be received by the State as a block grant. This would make the actual Federal revenues received subject to a State funding process, and the impact of this on total City revenues is uncertain.

In the opinion of PICA Staff, the potential impact of welfare reforms and implementation risks relating to IV-A revenue were the most substantial risks to overall General Fund revenue projections contained in the original draft of the Plan presented by the Mayor on January 26, 1995. At PICA Staff's request, the Plan was amended to reduce these risks by reducing General Fund projected DHS Federal revenues by $20 million annually in the FY97 through FY2000 period. DHS Class 200 obligations were reduced by the same amount in each year in the FY97-FY2000 period. The result is no change in DHS unreimbursed obligations, and no change in Plan projected fund balance.

However, the change reduces the risk that Federal DHS revenues will not be received as originally projected. The reduced obligation level is a realistic target, although it will require greater reductions from recent spending growth levels than originally projected. This obligation projection can be met if the process of management reform and increasing investment in prevention continue at DHS, and recent trends of reduced caseload growth continue.

Department of Public Health

**Proposed Medicaid Long Term Care changes --** ***The impact of the Governor's proposed changes in Medicaid reimbursements to long term care facilities on PNH and the City's obligations to the private operator of PNH contract is unclear***

The Governor's FY96 budget includes a proposal to shift reimbursements to nursing homes under Medicaid to a prospective payment system that would base reimbursements to nursing homes on average costs of similar facilities within regions, adjusted for the "case mix" of each facility, or the costs the facility could be expected to incur on the basis of the needs of its population. Under the contract with Episcopal Long Term Care, the private operator of PNH, financial obligations of the City may vary depending on changes in State Medicaid reimbursement. The impact of the proposed change in State Medicaid policy on City obligations under the PNH contract is a risk area.

**Impact of Federal and State Budget Cuts --** ***Various programs at the Federal and State level may be reduced and the City's ability to absorb these cuts without increases in local funding is uncertain.***

The Department has indicated that it is vulnerable to Federal and State funding cuts in various programs. State Act 152 funding for drug and alcohol treatment, Federal Ryan White AIDS treatment funding, and Healthy Start funding for pre- and post-natal care in Southwest and West Philadelphia, are among the programs that may be reduced. Total grant funding to DPH has increased dramatically in recent years, and grant funding now provides for over 85 percent of FY95 estimated DPH obligations in the General Fund and Grants Revenue Fund combined. The degree to which the Department can absorb significant cutbacks in grant funding without the use of additional local funds is uncertain.

Fire Department

**Overtime --** ***Mandated staffing levels requirements make it difficult for the Fire Department to control overtime costs***

As a result of arbitration proceedings the Fire Department was mandated to adhere to union requested minimum staffing level requirements. The Fire Department calculates that these mandates increased fire fighting staffing levels by 144 personnel and caused related personnel distribution problems and costs.

In the past, the Fire Department indicated that it anticipated recouping overtime costs through initiatives such the holiday buy back program. Unfortunately such initiatives results never materialized and overtime costs have continually escalated. Based on the City Quarterly Managers Report for the period ending December 31, 1994 Fire Department overtime was projected to be $2.3 million overbudget in FY95 with a net effect on overall Class 100 obligations of $836,523.

While PICA Staff feels comfortable with the Department's FY96 Class 100 projection, it continues to be concerned about the Department's inability to control overtime. Currently it appears that the Department is trying to minimize overtime effects by increasing savings in other areas. While this is an acceptable approach the City is very susceptible to costs overruns if these savings are not realized. Unless the Department is successful in its appeal of the arbitration award any assumption that departmental overtime costs will be effectively managed must be categorized as unduly optimistic.

Police Department

**Overtime Arbitration Ruling --** ***A recent ruling in favor of the FOP in an overtime arbitration dispute has negative implications for the City***

The following statement was included in footnote #28 to the City of Philadelphia's Financial Statements for Fiscal Year Ended June 30, 1994:

> "In November, 1989, an ACT 111 interest arbitration panel awarded the City Police Department a new shift schedule for uniformed employees. Pursuant to the award, police officers began working a new schedule effective January 5, 1990. As a result, officers who previously worked 2,085 hours spread over 260 8-hour workdays, now work 253 8 1/4 hour days. On January 9, 1990, the Fraternal Order of Police, Lodge No. 5 (FOP) filed a grievance asserting that police officers are entitled to 15 minutes additional pay on an overtime basis under the new 8¼ hour schedule. The City asserts that there is no requirement to pay any additional compensation since the new schedule awarded by the panel provides for officers to work fewer days and fewer

> hours per year because the officers' paid lunch period compensates for the time, and/or the Arbitration Award modified the contract. The City's exposure if the FOP were to prevail would be approximately $ 9 million per year for police personnel. The arbitration is scheduled to be held in the fall of 1994."

Recent accounts have indicated that the arbitration resulted in a ruling in the favor of the FOP, and that the City is in the process of appealing that decision.

The footnote further stated:

> "In August 1992, a group of current and retired police officers filed suit in Federal District Court challenging the City's pay practices, alleging that the City's failure to pay overtime for the extra 15 minutes per day of work required by the new schedule discussed above, and the City's failure to pay overtime compensation to police officers with the rank of Captain and above, violates the Fair Labor Standards Act ("FLSA"). The City has filed an Answer to the Complaint, denying all liability. Discovery has not yet to commenced. The City's liability, if plaintiffs were to prevail on all issues, is approximately $42 million. An adverse ruling would also substantially increase the City's overtime compensation costs going forward."

PICA Staff understands that, as yet, there has been no ruling on this matter.

While, the City indicates it is very optimistic that it will eventually prevail in both of the above matters , PICA Staff is very concerned as to the potential liability the City faces. Potential up front costs of $42 million with additional overtime costs going forward are not envisioned in the current Five Year Plan. Such a liability clearly would effect the City's overall General Fund budget adversely. PICA Staff will continue to closely monitor this situation.

Philadelphia Prison System

**Prison Food Service Contract -- *Prison food service costs increased due to unsatisfactory service by the previous vendor***

The Quarterly City Managers Report indicates that food service costs for FY95 will be $2 million more than initially projected because of unsatisfactory service from the previous vendor. In February 1995, the City increased the Department's food service appropriation to rectify this problem.

In FY96, or when the Curran Fromhold Correctional Facility comes on-line, the scope of the food service contract will drastically change. A new centralized kitchen facility will be brought on-line and the Prisons Department will begin its "chilled food initiative". This initiative contemplates that all prison facilities food will be prepared at one central facility and shipped to other locations for re-heating and serving.

While PICA Staff applauds the City's attempt to become more efficient in this area it is nonetheless a significant concern that neither the City nor the current vendor have experience in operating such a facility. This inexperience with a new technology causes PICA Staff to view projected food service costs as very speculative.

Public Property

**Philly Phlash Subsidy -- *The City's Philly Phlash subsidy to SEPTA is based on ridership participation***

As part of the most recent Five Year Plan, the City has included subsidy payments to SEPTA for the operation of the City's Philly Phlash historic/cultural area tourist buses. The City has indicated that a major factor in calculating this cost is ridership participation. The City has also indicated that current use of these vehicles is "expectantly" low; and if this trend continues subsidy payments will have to be increased in the out-years of the Plan.

**800Mhz Radio System -- *The City's 800Mhz Radio System continues to be a problem***

In our Staff Report on City of Philadelphia Quarterly Reports, dated December 30, 1994, PICA Staff extensively reviewed the City's communication system (based on information provided in its latest RFP for a 800Mhz system). The Department of Public Property has now indicated that it plans to award the contract by early spring with a projected completion date of two years.

While PICA Staff is pleased to see this portion of the project begin to take form, we are increasingly concerned about interim procedures being used until the new system is brought on-line.

In a recent meeting with Public Property, PICA Staff was advised that in order to resolve the current radio system problems the City would simply revise overall capacity; both by downsizing capacity of certain departmental users and by use of additional space that was recently located on the current system.

Public Property also indicated that it believed that removing old police radios and reinstalling them in vehicles such as sanitation trucks would be a cost effective method to eliminate the use of mobile phones, presently an additional cost to the City. Public Property management stated that they hoped to use this system for all sanitation vehicles in order that the system could operate efficiently. They did indicate, however, that the Streets Department would have the final say as what type of communication system it would utilize.

The Streets Department expressed no desire to utilize the Public Property "solution" to bring them totally on the radio system. They indicated an intent to expand the use of mobile phones to additional regions to the point where the department's fleet would ultimately utilize 50% mobile phones and 50% radios. The Streets Department indicated that their preference for 50% mobile phone utilization results from a lack of confidence in the

City's current communication system.  This lack of cohesive action between Departments causes PICA Staff grave concerns.

The major PICA Staff concern is the lack of centralized leadership over decisions concerning the City's mobile communication system.  The City has been successful in centralizing fleet and information services and it would seem logical that it would also be able to similarly resolve the mobile communication problem.  If it is the goal of the City to have a radio system in which all Departments can economically intercommunicate, individual departments should not be allowed to deviate from the primary mode of communication.

**Reporting Inconsistencies -- *The City continues to be inconsistent in reporting 911 proceeds***

In previous reports PICA criticized the City for being inconsistent in reporting 911 capital proceeds.  These inconsistencies continue in the FY96 Plan.  In the FY96 Capital budget the City projects receiving $5.8 million from 911 service charge fees, while for the same period in the General Fund the Plan only anticipates transferring $4 million to the Capital Fund.  PICA again encourages consistent reporting.

Streets Department

**Sick Leave Usage -- *Sanitation Division sick leave usage remains high***

Based on the Quarterly Managers Report for the six month period ending December 31, 1994 sanitation division sick leave usage was reported to be 8.1%.  The sick leave usage percentage is calculated by taking the number of sick leave days reported by a department and dividing it by the total number of days available to be worked in the period.  The City has determined the mid-point for sick leave of departmental averages to be 4.2% or eleven sick days a year.  At the current rate the sanitation division employees are averaging 21 sick days a year.

In a recent meeting, the Streets Department indicated the problem was twofold.  First, sanitation employees are consistently exposed to inclement conditions so they are more susceptible to illnesses, and second, abuse of sicktime remains high in the division.  The Department stated that its policy was to strictly enforce sick leave use policies, but questions about enforcement within the division were unsatisfactorily answered.  PICA Staff encourages the Department to develop and utilize enforceable procedures to manage sick leave usage.

Fleet Management

**Centralized Fleet Repair Facility -- *The City still has not located a Centralized Fleet Repair Facility***

Since the inception of the Office of Fleet Management, the Fleet Manager has stated that a key to the group's success is a centralized fleet repair facility. To date the Department has not been successful in obtaining a site. In meetings with PICA Staff and in testimony to City Council, the Fleet Manager has stated that one of the reasons overtime is high in his group is because of inadequate outdated garage facilities. He also indicated that at least two of his facilities have not been fully operational for an extended period of time. While he could not quantify an amount, he indicated that this situation has been very costly to the City.

**Inventory Control -- *Fleet Management continues to lack adequate inventory controls***

Another negative effect of not having a centralized fleet repair facility is the inability to properly control inventory. In recent meetings with the Office of Fleet Management, the vulnerability of the inventory control system was brought to PICA Staff's attention. While actual losses were not quantified by the Fleet Manager, he did indicate that they were substantial and that corrective action was sorely needed. PICA Staff encourages taking all the necessary steps to make improvements in this area.

## APPENDIX A

## Statutory Background, Plan Review Methodology and Summary of Events

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). 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, PICA Staff has included such information in this Appendix.

A brief summary of events to date including comments as to PICA's future focus, a summary of PICA Staff's Plan review methodology and a compilation of required future City reporting to PICA is also included.

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 to 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 1.5% 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.

Plan Review Methodology

Staff Report - The Plan was submitted to PICA on March 16, 1995 and the PICA Act provides a 30 day period for review which expires April 17, 1995. Authority Staff has consulted with the City, both on the departmental level and otherwise, since the Plan was submitted to City Council on January 26, 1995 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 PICA Staff. This report includes reference to materials received by the Authority through April 11, 1995.

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 consistently followed that requirement.

Relationship to Future Plan Revisions - The City is obligated under the 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 such matters within 45 days after declaration of a "variance" by PICA.

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, 1996 (100 days prior to the end of FY96). At that time, the City is required to add its Fiscal Year 2001 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.

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:

> Estimated 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.

Summary of Events to Date/Future Focus

PICA's creation was an action taken by the Commonwealth of Pennsylvania in direct reaction to Philadelphia's financial crisis. Accordingly, PICA's primary focus during its almost four years of existence has been to assist the City to avoid insolvency; to provide the funds directly required for that purpose and for essential capital programs; and to oversee the City's efforts to lay a sound foundation for its return to fiscal stability. The negotiation of the Cooperation Agreement to set out the basic terms of the City-PICA relationship, the PICA sponsored effort resulting in the establishing of the format and content of the Five-Year Financial Plan process, and the initial issuance of bonds to provide funds to assist the City to stabilize its finances were all major accomplishments. Subsequent successful defense against challenges to the constitutionality of the PICA Act was another vital PICA process component. PICA's annual assessment of Plan progress, successful annual challenges to initial Plan revenue estimates and suspect methodologies, evaluations of City reporting, and analysis of City practices and programs have assisted in the ongoing City improvement as envisioned by the PICA Act.

PICA also provides oversight as to the encumbrance by the City of in excess of $400 million of capital funds PICA provided for capital projects deemed required to rectify emergency conditions or necessary for Plan operational success. As indicated in the "Capital Program Office" section earlier in this report, PICA Staff has not been overly impressed by the City's management of capital programs. Improvements in this area have been fewer and less impressive than those witnessed in other facets of City overall operation.

To date, PICA has provided in excess of $1,058 million in funding to assist the City, allocated to the following purposes:

| Purpose | Amount (thousands) |
|---|---|
| Deficit Elimination/Indemnities Funding | $ 256,200 |
| Productivity Bank | 20,000 |
| Capital Projects | 400,773 |
| Refunding (retirement) of certain high interest City Debt | 381,300 |
| TOTAL | $1,058,273 |

PICA's authority to issue new money debt for purposes other than financing a City cash flow deficit expired as of December 31, 1994; thus PICA anticipates that its future activities will focus more closely on oversight on the City's efforts to maintain financial balance, further institutionalize management reforms (both those initiated to date and those still to be made) and to implement ongoing operations changes in accordance with a yet to be completed strategic plan.

Recent rating agency actions upgrading City general obligation bond ratings to investment grade (Moody's Baa/Standard & Poor's BBB-/Fitch BBB-) now allow the City, as envisioned in the FY1996-FY2000 Plan, to independently access capital markets. The timing of the upgrades validates the PICA process -- the City had taken advantage of the tools PICA made available to it. It is anticipated that the PICA/City relationship will continue to be a catalyst for further City operational improvements.

Future City Reporting to PICA

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 1996. 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 FY95 are May 15, 1995 and August 15, 1995. Quarterly reporting deadlines for FY96 are November 14, 1995, February 14, 1996, May 15, 1996 and August 15, 1996. 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 to be received relating to FY95 are: April 20, 1995 and July 20, 1995. For FY95 the reporting dates are October 20, 1995, January 22, 1996, April 22, 1996 and July 22, 1996. 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 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 FY95 is to be received on May 2, 1995. The

dates for submission of such reports for FY96 are August 1, 1995, November 1, 1995, January 3, 1996 and May 1, 1996.

# Pennsylvania Intergovernmental Cooperation Authority

**Staff Report**
**on the**
**City of Philadelphia's**
**Five-Year Financial Plan**
**for**
**Fiscal Year 1996 - Fiscal Year 2000**
**Incorporating Technical Modifications**
**as of July 12, 1995**

**July 17, 1995**

## INTRODUCTION

The City of Philadelphia, for the first time in PICA's operating history, has amended a proposed budget (amendment prior to the start of the fiscal year to which the proposed budget applies). Bills No. 1115, 1116, 1117 and 1118 approved by City Council and signed into law by the Mayor in June 1995 amended the fiscal year 1996 to fiscal year 2001 Capital Program and Budget; and Bills No. 1129, 1130, 1131 and 1132, similarly approved and signed, amended the City's fiscal year 1995 and fiscal year 1996 Operating Budgets.

The City (the Mayor) has accordingly provided to PICA, as required by the Intergovernmental Cooperation Agreement, a revised Five Year Financial Plan for Fiscal Year 1996 - Fiscal Year 2000 (including Fiscal Year 1995) Incorporating Technical Modifications required to make the Plan consistent with the above-mentioned recently adopted operating and capital budget ordinances.

PICA Staff has reviewed the Revised Plan and the related ordinances enacted during June 1995, and has determined that the technical changes from the original Plan approved by the PICA Board on April 17, 1995 are reasonable and appropriate and that they in no way adversely affect the Plan previously approved by the PICA Board.

Detail Provided Herewith

Provided herewith are PICA Staff prepared schedules which indicate the changes in the Operating Plan resulting from the technical modifications, the impact of the FY96 General Fund Transfer Ordinance, and the net effect of the modifications to the fiscal year 1996 Capital Program Budget. The modifications to the capital budget include the carryforward of previously approved funds (unutilized in prior year capital budgets) and should help improve the City reporting process.

Staff Recommendation

PICA Staff recommends that the Pennsylvania Intergovernmental Cooperation Authority approve the Revised Plan submitted by the City of Philadelphia -- the Plan formally titled:

City of Philadelphia
Five Year Financial Plan
Fiscal Year 1996 - Fiscal Year 2000
(including Fiscal Year 1995)

Fourth Five-Year Plan for the City of Philadelphia pursuant
to the Pennsylvania Intergovernmental Cooperation Act

Presented by the Mayor, January 26, 1995
Approved by City Council, March 16, 1995
Approved by PICA, April 17, 1995

Incorporating Technical Modifications as of July 12, 1995