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Improving Act 47: Expanding Municipal Options for Stabilization and Self-preservation

Act 47 is considered both needed, and avoided. On the one hand, a city acknowledges its shortcomings in tax base and revenue collection, and on the other, it is an admission of trouble. Act 47 guarantees state revenue to keep essential functions going. Yet, is the cure worse than the symptom?

Act 47 is an ironic corollary to Act 111.[1] Most pragmatic city governments see Act 47 as a way out of the draconian and restrictive provisions of Act 11, specifically the clause mandating binding arbitration by an appointed arbiter. Act 47 loosens some of these ties, most especially the disconnect between a city government's ability to pay a higher level of both wages and contracts. Like a citizen taxpayer, does a city have the duty to pay a cost for a contract for which it does not (in its assessed tax base or Act 511 receipts) have the resources to provide?

Pennsylvania's municipal unions have opposed Act 47 for some time to little avail. Without help from their putative natural allies, the Democratic urban leaders in the Pennsylvania Assembly or the Democratic governor, Rendell, the unions have seen their position somewhat weakened (although grandfathered contract and pension provisions still blow huge holes in agreements made before the realization of what the post-industrial era in Pennsylvania really meant). The objectively limiting powers of Act 47 to municipal unions have been the futile goal for defeat by these unions in both the legislature and the courts.

Politically, why should a Pennsylvania municipality accept Act 47 status? The mere action indicates instability and inability to deal with finances on an annual or ongoing basis. The perception to investors is plain: stay clear of here. The reception of the concept in the minds of those who wish for regional government, consolidation, or at the very least a COG[2] is "Go elsewhere and slip these chains."

Economically, Act 47 produces a neutral or positive bond rating due to increased leveraged power in contract negotiations, and the strengthened borrowing power in the light of state fiscal guarantees. Yet, the psychological damage and the market perception of an Act 47 city remain. How best to avoid these perhaps unfair perceptions?

The Center for the Study of Economics proposes several policy adaptations to Act 47 that can help empower designated cities to restructure themselves against several of the core conditions identified by the Pennsylvania Economy League as part of a "systemic problem" facing municipalities across the state.[3]

Recommendation 1: Change the tax structure

Clairton, Aliquippa, and New Castle are amongst a few other municipalities that were urged to get their fiscal house in order under Act 47 by the Commonwealth and its unofficial fiscal/policy enforcement arm, the Pennsylvania Economy League. Not only were they permitted by law to borrow, get state technical aid, and get wiggle room in contract negotiations, they were also urged—strongly—to adapt tax structures that were not based on the industrial realities of 1940s and 1950s Pennsylvania cities.

Therefore, in 1988 Clairton adopted reforms of its Act 511 tax rate levels but also the granddaddy of all taxes for localities—the real property tax. In these two cases, the DCA and PEL both recommended land value taxation,[4] as well as independent consultants, especially Mullin and Lonegan represented by the late Joseph Bendel,[5] mayor of McKeesport and board member of the Center for the Study of Economics. Aliquippa City's Revised Act 47 Recovery Plan of 2007 included LVT:[6]

> "The change in the form of government, which was approved by the voters previously, took effect January, 1988. It allowed the (now) City to implement a two-tier taxing system for real estate tax purposes and, by taxing vacant land at a higher rate than improvement, levy an even greater tax on [the LTV Mill] than the $338,000 budgeted in 1987. This tax has been paid but the continued success of this maneuver is not entirely clear. Therefore, although the 1989 and 1990 projections presented later in this report anticipate no change, there is the distinct possibility that, come 1991, the city will again have to make some extremely painful adjustments in order to maintain a balanced budget. It is the intention of the Coordinator that the recommendations presented in this plan will better enable the city to anticipate and meet those contingencies."

Have the intervening years changed the Act 47 recommendation at the time (1988)? No:[7]

> **Explore the issue of the advantages and disadvantage of the two-tier tax system that was implemented in 1988.**
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> **Update**: This study was requested by the City through a GCLGS Letter of Intent process and a professional peer consultant was assigned to the project through LGA Act 47 grant funds with oversight by the Center. The study was completed by Dr. Michael Weir, LGA, in order to review the impact of the two-tier land value tax. The study indicated that the shift to a level tax would negatively impact the residential tax burden for residents, especially high density buildings such as apartment buildings and townhouses. The tax would reduce the burden on the commercial and industrial properties where the land is not assessed at its true value. Should a county-wide assessment be undertaken by the Beaver County Commissioners, a new study should be conducted. The report was reviewed by the Manager & City Council on October 30 and a decision was made for "no change."
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> **Status**: Compliance

Recommendation 2: Require frequent revaluations

Counties lag in real property revaluation consistently across Pennsylvania. Outdated values cause the properties of poor, working, and middle-class households and businesses to become over-assessed relative to the rest of the county while the values of older but still desirable properties tend to remain under-assessed. This was the outcome in recent studies conducted in both the counties of Allegheny and Philadelphia.

Such distortions ultimately reduce the revenue collected in the affected cities, especially during years where the general level of real estate values rise, as happened in 2005-2007. Some of the increased value was captured through use of the real estate transfer tax, but only for properties that changed hands through market transactions. When the real estate market subsequently collapsed in 2008, transfer tax revenues dried up rapidly as sales of real estate shrank, forcing a new search for tax revenues.

Although looming lawsuits at the state level make it more likely that more frequent revaluations are going to be required, what happens to a Third-Class city that has old or inaccurate values in the meantime? Act 47 should require the home counties of designated cities to conduct a full revaluation to more fairly distribute the tax burden from the tax that is still the main source of same-city revenue: the property tax. If Harrisburg refuses to require full county revaluations, it should at least expand the existing right for a Third Class city to conduct a revaluation of its own to have the new values recognized for the full range of real estate taxation, including school district and county levies.

Recommendation 3: Allow innovative restructuring of the real property tax

Several additional tax tactics may be employed if the traditional land value tax, through either uncertain assessment or political realities, appears untenable.

Local options should be pursued that permit cities to also enact variations of LVT: A baseline dollar exemption for all taxable improvement, the revenue shortfall to be made up by raising the millage rate, referred to as assessment exemption for improvements (AXI). Research indicates that AXI is a progressive form of the property tax that provides powerful tax relief to those least able to pay for the increased revenues Act 47 cities need.

Also, cities must be able to apply a temporary separate user fee or charge on land values to augment the traditional property tax, referred to as the separate land value tax (SLVT). SLVT has the advantage of not punishing or discouraging new economic activity. In downtown CBDs, this tool can be used to create a special services district or business improvement district. This approach is already in use by the Downtown Pittsburgh Partnership in Pittsburgh's Golden Triangle, where commercial properties pay an annual levy against their land value to fund public safety and economic development efforts.

Recommendation 4: Reduce the amount of tax-exempt property

Third Class cities generally serve as the hubs of county, state, and federal government operations large educational, medical, and religious institutions and small non-profit organizations. Pennsylvania broadly exempts such property from taxation, causing cities to lose large portions of its tax base and the resulting revenue. Although there is a strong argument that the activity and presence of such entities contribute significantly to a city's quality of life in other ways, the growing costs of day-to-day operation of public services and infrastructure continually pressure cities to seek financial support from these entities.

The traditional approach of payments in lieu of taxes (PILOT) remains voluntary in the state, and broad support for expanded revenue sharing among surrounding jurisdictions that are currently subsidized by this situation appears slim. Cities under Act 47 should have special permission to tax currently exempt property, then, as clearly, balance of value traditionally provided by exempt entities is not enough to keep the city in operation.

Many states, such as Massachusetts and Vermont, provide total improvement exemptions for religious, educational, and medical institutions but the land remains taxable. By maintaining taxes on the land, it can help cities to finance the public services provided to these sites and capture the value created because of the services. In addition, it will help constrain the often-extensive use of land by non-profits, particularly in highly valuable locations such as hospital or university campuses. States such as Minnesota and Wisconsin have been aggressively evaluating such exemptions, and in Carbon County, PA the exemption status of churches being closed by Roman Catholic Diocese are being withdrawn.[8]

The challenges of 2009 and beyond

The recession of this year resembles in many ways the collapse of big Steel in the late 1970s and the recession of the early 1990s. Each time, land value taxation was adopted by struggling municipalities, not primarily as a way to cut taxes for struggling homeowners, but as a way to raise revenue from its only immobile tax base, maintain those revenues, and clear the decks for sustainable capital investment. Since then, cities that have flirted with insolvency (such as Washington, PA) have used LVT as a way to keep revenues stable while seeking a way out of the demographic and economic decline that have marked the Third Class cities of Pennsylvania.

We urge the members of the PLCM considering a way through recession to consider the one immobile tax base—land value—as a "go to" source of tax revenue, not for the political benefits it may or may not provide, but for the economic sense of gaining revenue through a publicly created resource. By unleashing the forces of the market while at the same time ethically collecting tax revenue that the community as a whole creates, the best aspects of urban life and economies are preserved without cost to the public treasury.

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[1] http://www.dli.state.pa.us/landi/lib/landi/laws-regulations\lmc\act111.pdf

[2] Council of Governments: Defined here as any association of independent taxing jurisdictions working together, with or without a common tax base to achieve a certain goal (i.e. Mosquito Control http://www.mwcog.org/news/press/detail.asp?NEWS_ID=59)

[3] *Structuring Healthy Communities: Municipal Case Studies.* Pennsylvania Economy League. March 2009.

[4] http://www.governmentlaw.org/files/landvaluetaxation.pdf

[5] http://www.post-gazette.com/obituaries/20031026bendelobit2p2.asp

[6] Aliquippa City's Revised Act 47 Recovery Plan. December 2007. http://www.newpa.com/get-local-gov-support/technical-assistance/request-assistance/act-47/download.aspx?id=482

[7] Ibid.

[8] http://lawprofessors.typepad.com/nonprofit/2009/02/closed-churches.html