BAILIWICK NEWS

Reporting and critical analysis of State College public affairs

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Municipal finance can-kickers running out of road.

By Katherine Watt

This is the second in an intermittent series on the 2017 State College budget. The first report was published on Sept. 23, 2016. I attended some but not all of the work sessions at which Borough Council reviewed specific sections of the budget. This report is mostly based on reading the proposed budget and thinking about it. Corrections and clarifications welcome – email kw.investigations.llc@gmail.com or use snail mail (below).

INTRODUCTION

Borough staff presented the 2017 municipal budget to the Borough Council on Oct. 21, and Council reviewed sections of the budget in work sessions during November. The public hearing was held Dec. 5, with additional Council discussion Dec. 6. Further discussion isscheduled for Dec. 12 and 13, and the adoption vote is planned for Dec. 19.

Dwight Miller, Manager of Financial Services for the Borough of State College, opened a Budget 101 public education meeting on Sept. 9 by identifying two goals for the workshop series: educating the public about budget issues, and engaging the public in discussions about future taxing and spending decisions.

Miller explained that a municipal budget serves three purposes. It's a policy document that presents Borough Council's priorities to the public. Because resources are not infinite, Council must select which programs get funded, and which don't. Second, it's a plan that explains how Council goals will be achieved, and monitors public employees' progress toward meeting those goals. Third, it's a legal document that authorizes Borough staff to spend public money to provide the selected public services.

Public employees, including Miller, are working to increase public engagement with the budgeting process, not out of some fuzzy interest in general civic education, but because State College is facing serious budgetary gaps between revenue and expenses, and not in the good way.

As reported by *Bailiwick News* Sept. 23, for the last decade, revenue has been consistently less than expenses. This trend is driven by the build-out of the Borough (little room to add more taxable real estate to the property tax rolls) and the displacement of wage-earning adults with low-income Penn State students (lowering earned income tax revenue), as wage earners move to the suburban townships, and corporate Penn State continues to increase undergraduate enrollment without increasing on-campus housing. Other budget gap drivers include rapidly rising costs for health care and pensions for public employees.

Taxpaying citizens need to be involved in detailed public budget discussions so that when the time comes to cut services, raise taxes, or both, people know what's happening, why it's happening, and have had a voice in deciding which programs and services to cut or eliminate and how much, how fast to raise taxes.

There's a political gap to go along with the budgetary gap. Staff members communicate regularly with Borough Council – the legislative body that legally adopts the annual municipal budget. Staff members communicate as much as possible with taxpaying citizens, collecting input from participants in the Budget 101 sessions and through online and handwritten public comment depositories.

But there is currently no mechanism to facilitate multilateral discussion about budgetary issues among the three stakeholder groups: Council members, public employees, and taxpaying public.

There's also a knowledge gap. A major block to increased citizen engagement is the complexity of the budget: the way in which departments, divisions and funds are dispersed and networked together through the budget document.

It's too late to set up such a multilateral discussion mechanism for the 2017 budget cycle, but *Bailiwick News* will continue to collect, analyze and disseminate information about public spending next year, and will advocate for multilateral meetings to begin during the 2017 preparation cycle for the 2018 budget.

Budget Structure

The State College budget includes sixteen "funds." A fund is defined in a July 2015 State College budget presentation as "a fiscal and accounting entity with a self-balancing set of accounts...for the purpose of carrying on specific activities or attaining certain objectives…[used to] keep track of the assets, liabilities, revenue, expenditures, and fund balances related to [those] activities."

These 16 funds fit together like puzzle pieces to account for the projected $48.6 million that will flow through public coffers next year.

There are four "Governmental" funds. The General Fund is the largest single fund at $27.6 million; it covers operational costs for the six main governmental departments and is primarily supported by property and earned income taxes. The General Fund is structurally balanced in the proposed 2017 budget: revenues and expenses are projected to match.

However, the General Fund is only a portion of the total $48.6 million budget. There's another $21 million accounted for in other funds.

The Capital Fund (the second Governmental fund) pays for maintenance of public buildings and streets. The Capital Fund been underfunded for at least the last ten years, leading to deferred maintenance of public infrastructure. As a result, finance staffers are projecting a $1.9 million annual gap between maintenance needs and available funds for the next five years; they recommend Council consider and adopt a phased 4.4 mill property tax increase (1.1 mill per year between 2018 and 2021) to fill the hole. That discussion is not part of the imminent adoption of the 2017 budget. If Council takes up the tax increase proposal at all, it will be subject to separate public hearing procedures in the future.

The two other Governmental funds are the Insurance Reserve Fund, used to offset annual increases in employee contributions to health care premiums, and the Asset Replacement Fund, used to replace vehicles and computers as they wear out.

There are six "Enterprise" or "Proprietary" funds, treated more or less like businesses. Fees paid into the fund by service users mostly cover the costs of providing those services. The Enterprise funds include the Sanitary Sewer fund (sewage pipe operation and maintenance); Refuse fund (trash collection); Compost fund (compost collection); Parking fund (off-street parking facility operations), Centre Tax Agency fund (county-wide tax collection services); Bus Terminal; and Bellaire Court (public senior housing).

There are three "Special Revenue" funds, primarily supported by state and federal grants. These include the HOME fund (part of Housing and Urban Development), the Highway Aid fund, and the CDBG (Community Development Block Grant) fund.

There are two "Component Unit" funds: the CIDA fund (Commercial and Industrial Development Authority) and the Redevelopment Authority fund. The Redevelopment Authority's mission is blight elimination. In recent years, RDA members have mostly worked on the Homestead Investment Program (HIP) to stabilize neighborhoods that are at risk of destabilization from increasing student rental density, by encouraging more long-term residents. Next year the RDA will continue HIP work, and also work on commercial redevelopment of the 200 block of South Allen St., between Allen Street, D Alley, Highland Alley and Foster Street.

There is one "Internal Service" fund. The Fleet Services fund is used to repair and maintain public vehicles.

Administrative Structure – Departments & Divisions

The General Fund covers operating costs for six departments: 1) Police; 2) General Administration; 3) Public Works; 4) Planning; 5) Neighborhood & Community Services and 6) Parking.

The Police department includes patrol and detective divisions, plus a professional standards division. The Police department has been coming in under budget in recent years, primarily because there are several unfilled officer positions, lowering labor costs. There are currently about 60 funded officer positions, although a 2012 public safety study recommended that, due to the high proportion of young residents between 18 and 24, the Borough should have about 70.

General Administration includes four local taxpayer-funded divisions: Administration; Financial Services, Tax Collection and Information Technology, plus one division (Centre Tax Agency) that collects earned income taxes within Centre County, and is primarily funded by commissions paid by participating municipalities and school districts.

The Public Works Department includes 10 divisions: Administration; Municipal Facilities division (maintains public buildings); Streets division (maintains public streets); Trees & Parks division (maintains public trees and parks); Sanitary Sewer fund (operates and maintains sewage pipes); Refuse fund (collects trash); Compost fund (collects compost); Bus Terminal fund (maintains the downtown bus station); and Fleet Services fund (maintains public vehicles).

The Planning Department includes three divisions. Planning & Zoning staff primarily review incoming development applications to assess compliance with existing zoning regulations and shepherd the applications through the Planning Commission and Borough Council approval process. They also research and prepare drafts of new regulations for Council adoption.

Housing & Community Development staff members manage public senior housing (operated through the Bellaire Court enterprise fund), and also support the Redevelopment Authority, which works on blight elimination. The third Planning division – Economic Development – has been inactive the last few years, because there haven't been funds to hire someone to work on it. Planning Director Ed LeClear said, at a Nov. 21 Council work session, that his goals for 2017 include supporting the comprehensive overhaul of the State College zoning code (last done in 1959) and developing an information campaign to educate the public about the variety of local housing-related programs.

The Neighborhood and Community Services Department includes two divisions: Health Code Enforcement, inspecting restaurants for health code compliance and properties for enforcement of weed, snow, and trash removal rules; and Community Engagement, which handles programs to alleviate town-gown tensions.

The Parking Department includes two divisions: Parking Enforcement (issuing tickets for violations of parking rules) and the Parking fund, which uses income from parking fees at public off-street parking decks, garages and lots, to maintain and operate those facilities.

Revenue

On the revenue side, in 2017 the General Fund will take in about $7.5 million in real estate taxes collected from people who own property in the Borough, except Penn State, K-12 schools, and religious organizations, which are tax-exempt. Property taxes account for about 27% of the total revenue collected to support General Fund services.

Sales of contracted services include work performed by Borough employees for other entities such as Harris Township (accounting) and Centre Region Council of Governments (information technology), are projected to bring in about $6.5 million (23%).

Earned income taxes paid by wage-earners who live in the Borough will contribute about $4.7 million (17%). Real estate transfer taxes are expected to raise about $1 million. Local services taxes (a flat tax levied on people who work in the Borough, even if they live elsewhere) are expected to bring in about $1.2 million.

The rest of the revenue will come mostly from fines for ordinance violations; user fees; license and permit sales; grants; interest income, and rent collected on public spaces rented out to private entities.

Penn State will contribute about $642,000 to the Capital fund, as a fee-in-lieu of real estate taxes. This amount is negotiated every 20 years; we are currently at year 10 in the cycle. For reference, Penn State's property within Borough boundaries was assessed at about $262.9 million in 2015. According to a Frequently Asked ➚ Question page at the Borough's website, if that property were taxable, the resulting 2015 real estate tax payment would have been about $3.8 million. Thus, corporate Penn State enjoys a tax savings of $3.2 million per year by classifying itself – for property tax purposes at least – as a public institution.

I plan to investigate further to find out about the law authorizing the negotiation process, whether the next negotiation begin sooner by Council action, and if so, whether Council has the political risk appetite to push corporate Penn State for a significant increase in the annual fee-in-lieu contribution.

Expenses

On the General Fund spending side, about $10 million will pay for police protection. About $6.1 million will pay for public works. About $4.4 million will pay for administration. About $3.5 million will go to debt repayments; under our current debt load, this annual expense rises to about $3.9 million in 2025, before tapering down to about $1.4 million in 2033 and being paid off in 20134. About $1.78 million will go to regional programs (see table). About $978,000 will pay for planning programs.

2017 GENERAL FUND EXPENSES (Top 6 Expenses)	Dollar Amount (rounded)	Portion of Total General Fund Expenses	PAGE CITATION
Police Protection	$10,000,000	36%	p. 185
Public Works	$6,100,000	22%	Multiple
General Administration	$4,400,000	16%	Multiple
Debt Repayment (prior borrowing)	$3,500,000	13%	p. 42
Regional Programs	$1,780,000	6%	Multiple, see below
Planning Department	$978,000	5%	p. 151

Centre Region Council of Governments Contributions	Dollar Amount	Portion of Total COG Contribution ($1,775,218)	Page Citation
Parks & Recreation Programs	$622,812	35%	p. 270
Firefighting Services	$546,213	31%	p. 258
Schlow Library Services	$446,753	25%	p. 264
CATA Bus Services	$132,428	7.5%	p. 267
Emergency Management Services	$27,012	1.5%	p. 261

COMPLEX NETWORK

The networking of the various budgets makes it very difficult for non-accountants – and probably even for accountants – to "follow the money" and get a clear sense of how much each program costs to operate.

Within the State College budget, there are many interfund transfers between departments. For example, several departments "pay" the public works department for work the public works employees perform for other programs.

Some services are outsourced to private contractors, such as management of the public employee pension funds.

There are intergovernmental transfers between municipalities. For example, Harris Township pays State College for accounting services, and College Township pays State College for police services.

There are intergovernmental transfers between COG and municipalities. COG pays State College for information technology services, and State College pays COG for library services.

The State College Borough Water Authority gets funding from users, but with a pass-through. State College households and businesses send payments for water service to the Borough. The Borough then submits aggregate payments to the water authority.

Public borrowing adds another layer of complexity. When the Borough, or a regional entity of which the Borough is a part, borrows money from a bank or through the sale of municipal bonds, that money counts as current "revenue." But unlike tax dollars, debt funding must be repaid with interest to the lenders over ensuing years. It's a tax on future residents, incurred by current and past residents.

Different departments within a single entity occasionally lend money to each other. For example, the Centre Region Code Agency currently has a large fund surplus due to the recent construction boom and related permitting fees paid by developers. The code agency is not funded by direct municipal contributions.

Because of the surplus money in the code agency "new construction" account, within the 2017 COG budget, the code agency will loan about $250,000 to the Centre Region Parks & Recreation Authority, for cost overages for the Oak Hall Regional Park project, and for the senior center's sequential moves to two Nittany Mall locations. The Parks Authority will pay back the debt, by collecting municipal contributions from regional taxpayers, for the next seven years.

Thus, when a citizen taxpayer looks at local budgets to find out how much it costs to have the programs we currently have, and how the incremental costs relate to potential upgrades or downgrades in services, those answers are unclear at best. It's not because public employees are trying to con taxpayers, but because over time, public systems have become extremely complex and networked.

CRITICAL ANALYSIS

Proponents of increased complexity and centralization often suggest that there are efficiencies of scale to be realized: it costs less for each participant in a pooled program than it would for the participant to operate a stand-alone program. The corollary is that there is a point of diminishing returns, when maintenance of the complexity costs more than savings from the pooling.

We're somewhat beyond that point, in my view.

I look at municipal economics through the lens of catabolic collapse, derived from analysis by John Michael Greer, Charles Hughes-Smith, David Stockman, Brandon Smith, Chris Martenson and a handful of other socioeconomic analysts. They generally argue that the 2007-2008 financial crisis was a small bump down the prosperity gradient; there has not been a genuine economic recovery – only a reinflation of the stock bubble; and the next, larger bump down the gradient is immediately ahead.

The proximate trigger will likely be an increase in interest rates by the Federal Reserve. But the long-term driving force is the depletion of cheap, easy-to-access fossil fuel reserves and the energy subsidy they've provided to economies. Quantitative easing was a global can-kicking strategy, not a fix. The capital mal-investment and currency debasement that accommodative monetary policies have teed up will be ugly in the unwind.

Catabolic collapse is an idea developed by Greer in a 2005 academic paper. It's basically economic cannibalism, or put more mildly, scaling back expectations to align with resources. Stressed communities throughout history, if they're sensible, dismantle what their members designate less-essential, unaffordable infrastructure, freeing up scarce resources to maintain more essential infrastructure.

One example often cited by Greer is the "Rust Belt" of the United States. Factories, farms, and the people who worked at them, were both abandoned by our national society in 1970s as we turned to cheap foreign labor to produce goods for import. It's debatable whether that was a sound choice. We "invested" the savings in complex financial instruments like mortgage-backed securities.

In line with these multi-decade national trends, corporate Penn State has increased undergraduate enrollment, and the Centre Region has crafted zoning policies to encourage the construction of new housing and commercial properties on former farmland and forests. We've made large resource investments in building and maintaining paved roads, to facilitate vehicular traffic. We've upgraded the technical complexity of our water and sewer systems to support increased population.

If, as catabolic collapse theory suggests, recent political upheaval is just one more symptom of an over-stretched, fraying social fabric, then local communities would be well served to make upcoming local decisions as if state and federal financial and logistical support will be dwindling further, to negligible levels.

This may indicate a public need for decentralization and simplification, sometimes called re-localization, to create redundant, locally-controlled, low-tech, small-scale systems producing safe water, food, housing, essential durable goods, health care, public safety, education, and employing the people who provide those goods and services.

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