COMMONWEALTH OF PENNSYLVANIA
HOUSE OF REPRESENTATIVES
HOUSE FINANCE COMMITTEE

IRVIS OFFICE BUILDING
ROOM G-50
HARRISBURG, PENNSYLVANIA

MONDAY, AUGUST 18, 2008
1:07 P.M.

BEFORE:

HONORABLE DAVID K. LEVDANSKY, MAJORITY CHAIRMAN
HONORABLE STEVEN R. NICKOL, MINORITY CHAIRMAN
HONORABLE WILLIAM C. KORTZ, II
HONORABLE DARYL D. METCALFE
HONORABLE STEVEN W. CAPPELLI
HONORABLE BRIAN L. ELLIS
HONORABLE C. ADAM HARRIS
HONORABLE DAVID R. KESSLER
HONORABLE DAVE REED
HONORABLE CHRIS SAINATO
HONORABLE DANTE SANTONI, JR.
HONORABLE MARIO M. SCAVELLO
HONORABLE TIM SEIP
HONORABLE RANDY VULAKOVICH

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ALSO PRESENT:

ROBERT KASSOWAY, MAJORITY EXECUTIVE DIRECTOR

ANDREW RITTER, MINORITY EXECUTIVE DIRECTOR

ERIC MOCK, MAJORITY RESEARCH ANALYST

BRENDA J. PARDUN, RPR
REPORTER - NOTARY PUBLIC

INDEX

CHAIRMAN LEVDANSKY: Good afternoon.

Today's hearing is on Senate Bill 961, legislation to authorize an additional earned income tax levy for the City of Hazleton under Act 511.

It is the intention of this legislation to substitute this tax for the current levy being paid by Hazleton taxpayers under Act 205, the Municipal Pension Plan Funding Standard and Recovery Act.

Under that act, municipal pension plans are categorized as to the degree of distress by a series of formulas laid out in the act.

Three levels of distress were outlined in the act: minimal, moderate, and severe. Each level had options that a municipality could take to address its pension financial status. One of these options was to exceed any statutory limitations on the rate of taxation on earned income or property taxes.

The revenue generated by the additional taxation on earned income and property could not be used to replace any current general fund revenues that were being used to fund the pension, and they could not be used to increase any benefits under the pension plan.

The Auditor General's office, during their recent audit of the pension system as provided by Act 205, discovered what they considered a violation on the prohibition of the use of these tax levies under Act 205 and issued an opinion that the funds that were misused to be paid back to the pension fund for its normal obligations.

The hearing today is, in essence, a fact-finding initiative to acquaint committee members and the public with the issues surrounding the situation and the suggested legislative remedy.

We've asked a number of people to testify. And before we begin the testimony, let me request that those of you that testify, I'd appreciate if you could stay for the remainder of the hearing, because likely members will have questions. And it may be beneficial and helpful for you to stick around. We may want to readdress some questions to the people that testify at the beginning. Okay?

With that, I'd like to call Mr. James McAneny, the executive director of the Public Employee Retirement Commission.

Mr. McAneny, before you get started, let me also ask the members of the committee to introduce themselves, starting with my colleague to my left, Representative Nickol.

REPRESENTATIVE NICKOL: Representative Steve Nickol. I represent Adams and York Counties.

REPRESENTATIVE CAPPELLI: Representative Steve Cappelli from Lycoming County.

REPRESENTATIVE SCAVELLO: Good afternoon. Representative Mario Scavello from Monroe. I will be stepping out for a few minutes, Mr. Chairman, but then return. I have another committee meeting.

REPRESENTATIVE SANTONI: I'm Dante Santoni from Berks County.

REPRESENTATIVE KORTZ: Good afternoon. I am Representative Bill Kortz from Allegheny County, 38th District.

REPRESENTATIVE VULAKOVICH: Randy Vulakovich, 30th District, Allegheny County.

REPRESENTATIVE KESSLER: David Kessler, Berks County.

REPRESENTATIVE SEIP: Tim Seip, representing parts of Schuylkill and parts of Berks County, the Yuengling and Cabela district.

REPRESENTATIVE SAINATO: I'm Representative Chris Sainato. I represent the 9th Legislative District, which includes a good portion of Lawrence and a small section of Beaver County.

REPRESENTATIVE HARRIS: Representative Adam Harris. I represent the 82nd District, which is all of Juniata and parts of Mifflin and Snyder.

REPRESENTATIVE ELLIS: Representative Brian Ellis, 11th District, Butler County.

REPRESENTATIVE REED: Dave Reed, Indiana County, 62nd District.

CHAIRMAN LEVDANSKY: Thank you.

Mr. McAneny, welcome.

MR. MCANENY: Thank you. I would like to thank Chairman Levdansky and the other honorable members of the House Finance Committee for providing this opportunity to address the special taxing authority granted to certain municipalities with distressed pension plans, the problem disclosed by the audit of the City of Hazleton and the resolution of that problem by Senate Bill Number 961.

The Municipal Pension Plan Funding Standard and Recovery Act, basically known as Act 205, requires the normal cost and administrative expense requirements and the amortization contribution requirement for the following plan year, less member contributions, to be paid annually to the pension plan from the revenue of the municipality. That's the statutory language.

Act 205 further provides for state aid to help defray the employer's obligations to those pension funds. And last year it was somewhat in excess of $206 million that the State provided to help fund pensions in Pennsylvania.

Section 607 of Act 205 provides remedies applicable to various recovery program levels in municipalities whose pensions qualify as distressed. Section (B) provides for the aggregation of the different municipal pension plans for purposes of investment and administration.

Subsection (C) and (D) permit member and employer contributions to exceed the limits imposed by other laws.

Subsection (E) provides for the establishment of a revised benefits structure for newly hired employees.

Subsections (G) and (H) allow extended amortization periods for the payments of certain liabilities.

And Subsection (F) permits the exercise of the special taxing authority.

The process for designating new municipal pension plans as distressed expired on December 31st, 2003. So only previously designated pension plans have access to those special provisions.

For those who may wish to know, there were 52 municipalities that originally submitted for and were designated as the distressed. Nine since have declared full recovery and withdrawn from that. So there are 43 remaining municipalities that would qualify to utilize the Act 205 tax.

The special tax permitted by Section 607(F) of Act 205 was designed to avoid a financial crisis in municipalities that had funded their plans on a pay-as-you-go basis. It can only be imposed by municipalities with an underfunded pension system that is already at its taxing authority limits, and can only be used to pay required costs directly attributable to Act 205's required maintenance of the municipal pension plan.

The language of the act is: If the tax rates set by the municipality on earned income or on real property are at the maximum provided by application and law, the municipalities may increase its tax on either earned income or real property above those maximum rates. The proceeds of this special municipal tax increase shall be used solely to defray the additional costs required to be paid pursuant to this act which are directly related to the pension plans of the municipalities.

So both the authority to impose the tax and the amount of the tax are dependent upon the new financial burden created by Act 205. Therefore, the current statute precludes the use of the special tax proceeds for post-retirement medical benefits, as they are not additional costs required to be paid under Act 205.

If a municipality needs additional tax revenue to pay for those benefits, it would need to seek judicial approval to exceed its general taxing authority pursuant to the Earned Income Tax Law.

What the Auditor General discovered was that Hazleton was assessing a special earned income tax under the auspices of Act 205, but was utilizing a substantial portion thereof to fund post-retirement medical insurance benefits rather than pension costs required to be paid by Act 205.

Another portion of that money was being used to pay for accumulated leave buyout. If someone had accumulated annual and sick leave, it was going to paid out at -- bought out at the time of retirement, that money was being used for that purpose too, but the dollars aren't nearly as big.

Act 205 is exclusively limited in its operation and effect of public employee pension requirement plans, whereas retiree healthcare is properly characterized as other post-employment benefit, or OPEB. Historically, medical insurance benefits have not been viewed as retirement allowances or pensions but is contract benefits earned now but with a deferred receipt, and based upon entirely different statutory authorities.

Likewise, the Government Accounting Standards, GASB, clearly recognizes the distinction between pension benefits and post-retirement medical benefit as stated in the introduction to GASB Statement No. 45, issued June 2004: In addition to pensions, many state and local government employers provide other post-employment benefits, OPEB, as part of the total compensation offered to attract and retain the services of qualified employees. OPEB includes post-employment healthcare as well as other forms of post-employment benefits, for example, life insurance, when provided separately from a pension plan. This statement establishes standards for the measurement, recognition, and display of OPEB expenditures and related liabilities, assets, note disclosures and, if applicable, required supplemental information in the financial reports of state and local government employers.

The approach followed until this Statement generally is consistent with the approach adopted in Statement No. 27, Accounting for Pensions by State and Local Government Employers, with modifications through to reflect differences between pension benefits and OPEB.

Statement No. 43, Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans addresses financial statements and disclosure requirements for reporting by administrators or trustees of OPEB plan assets or by employers or sponsors that include OPEB plan assets as trust or agency funds in their financial reports.

Now, we are aware of the recent decision of the Commonwealth Court in <u>Danzille</u>

v. Lomeo, 944 A. 2d 813, that just came out this year, which seems to suggest that post-retirement medical benefits are pension benefits under Act 205, but that case dealt with the issue of investment authority of an OPEB trust, however, and neither the Commission nor the Department of the Auditor General believe that it should be accepted as precedential regarding the distinction between pensions and other post-employment benefits as it would impose the actuarial reporting and funding standards of Act 205 on all municipality post-retirement medical benefit programs, including Hazleton's.

The immediate fiscal impact upon Pennsylvania local governments would be catastrophic and was certainly not within the contemplation of the court.

It should be noted that the trial court did not address that issue. Neither party argued or briefed that issue. It was brought up entirely sua sponte by the judge in the Commonwealth Court that wrote the opinion.

So there was never any real analysis

of it. It just seemed like a good idea so it showed up in the opinion. But I don't believe it's meant to hold that post-retirement medical benefits are, in fact, the same as pension benefits subject to Act 205.

The General Assembly has seen fit to limit municipal taxing authority through Sections 8 and 17 of the Local Tax Enabling Act, which provides Section 8, Limitation on Rates of Specific Taxes: No taxes under the provisions of this act shall be levied by any political subdivision on the following subjects exceeding the rates specified in this section: on wages, salaries, commissions, and other earned incomes of individuals, 1 percent.

So we have a 1 percent cap on earned income tax.

Section 17, the Overall-Limit on Tax Revenues: The aggregate amount of all taxes imposed by any political subdivision under this section and in effect during any fiscal year shall not exceed the amount equal to the product obtained by multiplying the latest total market valuation of real estate in such political subdivision, as determined by the board of assessment and revision of taxes, or any similar board established by the assessment laws which determines market values of real estate within the political subdivision by twelve mills.

So we have the combination of real estate and earned income tax limited by act of the General Assembly.

In financially troubled municipalities, however, special provisions of Section 123 and 141 of the Municipalities' Financial Recovery Act, known as Act 47, allow municipalities to exceed those statutory limits with court approval.

Powers and duties of municipalities, the right to petition the court for a tax increase: After a municipality has adopted a plan under Subchapter C of Chapter 2, it may petition the Court of Common Pleas of the county in which the municipality is located to increase its tax -- its rates of taxation of earned income, real property, or both beyond the maximum rates provided by law.

And jurisdiction of the Court of

Common Pleas allows the court to act upon that petition to increase the tax rates.

Notably, the only earned income taxes that could be assessed upon nonresidents of the municipalities other than Philadelphia are those imposed pursuant to Act 47, except where the municipality of residence does not assess the tax. If there is no income tax imposed by the municipality of residence, the municipalities where you work can assess the tax and keep it as opposed to assessing the tax and having to send it to the municipality of residence.

But it's still limited to the one percent. It doesn't go beyond that.

So although Act 205 does not address extending taxing authority over nonresidents, Hazleton imposed the Act 205 tax on nonresidents who work within the city. We anticipate finding that other municipalities are doing the same.

Although it is not necessarily an issue of direct concern to this commission, the subject of government transparency should also be considered. While municipality taxing authority is generally limited by statute either by specifying the allowable tax rate or by requiring voter or court approval to exceed those rates, the special tax provisions of Act 205 circumvent those proceedings, but only under very limited circumstances and for a specific purpose designed to address a compelling need.

The amount of the Act 205 tax is limited by the amount needed to satisfy the municipality's immediate statutory obligation to the pension. But otherwise, it's not limited. Theoretically, this could be a 10 percent income tax, if that was the requirement to fund the Act 205 financial requirements for that year.

We also note the potential for the impairment of a pension fund status under the Internal Revenue Code if nonpension benefits are payable from the fund. While government plans are rarely subjected to close scrutiny, the risk of losing a plan's deferred tax status is substantial, and the IRS has just recently announced its intention to address what it called underserving of government pensions in the immediate future.

It is necessary to maintain the clear distinction between retirement benefits that are payable from the qualified pension plan and OPEB liabilities that should be funded from another source.

Hazleton is one of 11 municipalities that have reported to the Department of Community and Economic Development that they impose a tax under the authority of Act 205, and the list is on page six. However, two of those municipalities were never certified as distressed prior to the expiration of 2003, which raises questions as to their entitlement to utilize the special relief of distressed municipalities under Act 205.

And since the actual application of the tax revenues is not reported at DCED, it cannot be determined from available information whether any of those municipalities use Act 205 taxes to fund anything other than the permitted minimum financial requirements of their pension plans. Only in audits such as the one that disclosed the Hazleton situation can ultimately determine the facts.

It must also be noted that not every municipality reports the statutory basis of its taxes to DCED, so it is possible that additional municipalities may be identified in the future. And there are 22 municipalities that do not advise DCED of their taxing authority, and yet the numbers would indicate that they exceed the 1 percent earned income tax rate without any other authority that's obvious, like their home rule or under Act 47.

In the current decade, Hazleton has received more than $3.3 million in State pension aid as follows. We have from 2000 through 2007 the amounts that have been paid.

In comparison to other third-class cities, Hazleton is neither the best nor the worst in terms of pension solvency. If you look at pages eight -- which page eight is Hazleton, and the rest of the pages through 19 are comparisons to other third-class cities.

For 2007, the police pension is 70 percent funded, the firefighter's pension is 76 percent funded, and its nonuniformed employee plan is 91 percent funded. This would place Hazleton in the upper-middle grouping, but actually Hazleton is doing better than the numbers suggest.

Thirteen of the cities on that list have issued pension bonds that shift financial obligations from their pension funds to their general funds, which tends to distort the real financial obligation of the city for pension benefits directly or through payment of the bond obligations. And page seven shows the cities with the bonds and the amounts.

But Hazleton's comparative status to other municipalities is really not the issue here. Because Act 205 tax is not being used to fund pension liabilities, and Senate Bill Number 961 is not pension legislation. Rather, Senate Bill 961 is a municipal tax provision that would allow access to additional taxing authority to pay OPEB costs in lieu of the inappropriate use of the Act 205 tax. So it is a shifting; it is not a new tax.

Further, Senate Bill 961 would establish a procedure to obtain judicial approval and allow for public disclosure, as opposed to the current method under Act 205 where the municipality just imposes the tax and there's no supervision or public view of that particular action.

We believe that Senate Bill Number 961 provides a better way to provide for Hazleton's financial needs than the method currently being employed. It would resolve the issue of misuse of the special tax provisions of Act 205, and it would resolve the audit finding based thereon.

Any questions?

CHAIRMAN LEVDANSKY: Thank you, Mr. McAneny.

Any questions from the members?

Representative Vulakovich.

REPRESENTATIVE VULAKOVICH: Just to get this clear, what they have been doing is paying certain benefits out of their pension plan that they should not have been?

MR. MCANENY: No. No. This is not money being paid from the pension plan.

REPRESENTATIVE VULAKOVICH: Not the legislation. What have they been doing wrong?

MR. MCANENY: Okay. They have imposed a tax which is allowed by Act 205.

REPRESENTATIVE VULAKOVICH: Right.

MR. MCANENY: And Act 205, the tax is designed to provide municipalities a way to fund the Act 205 requirements that they hadn't been doing before it was passed.

So what they did in Hazleton was to assess the tax, but instead of providing the proceeds from the tax to the pensions, they applied the proceeds -- not all of them, some of the proceeds of the tax to paying for other benefits, post-retirement medicals and leave payout. So the money was not taken from the pension plan; it never made it to the pension plan.

REPRESENTATIVE VULAKOVICH: None of the money ever did.

MR. MCANENY: Some of the money that was collected under the tax did go to the pension plan, and nobody's challenging that. That's not the basis of the audit finding or the problem with this legislation.

REPRESENTATIVE VULAKOVICH: My other

question was: But they would not have qualified for -- to be able to do this in the first place because they would have to be distressed; right?

MR. MCANENY: They were a municipality who qualified for distress under the pension statute, under Act 205. That's not the same as Act 47 distress.

REPRESENTATIVE VULAKOVICH: Okay. But they were 70 percent funded for police, 76 funded in firefighters, and 91 percent in their nonuniformed; that's pretty good.

MR. MCANENY: That's actually pretty good. But back when the action was first taken, Hazleton applied for its distress classification back in -- well, the number I have was in the '87, '88 year, and at that point the distress score was fairly low. They were not a terribly distressed plan even then, but it was still sufficient to be distressed under the statute.

And you'd have -- we'd have to sit down and go over the actual formulas to show you where the numbers were, but they were qualified under the act.

REPRESENTATIVE VULAKOVICH: Well, this bill specifically helps them; right?

MR. MCANENY: Yes.

REPRESENTATIVE VULAKOVICH: It wouldn't help anyone else at this period of time?

MR. MCANENY: With the -- with the language in the bill that was added, it deals with census. It would only -- that limits it to Hazleton, as I understand it. The census limitation would restrict it to Hazleton.

REPRESENTATIVE VULAKOVICH: Thank you.

CHAIRMAN LEVDANSKY: We have been joined by Representative Metcalfe from Butler County.

Questions from other members?

Representative Scavello.

REPRESENTATIVE SCAVELLO: Thank you, Mr. Chairman. First, I apologize because I had to step out for part of your testimony.

I notice this is a Senate bill. Was there a hearing held in the Senate? How does the bill stand over in the Senate right now?

MR. MCANENY: This bill passed the

Senate, I believe, 49 to 1.

REPRESENTATIVE SCAVELLO: Forty-nine to 1.

MR. MCANENY: And there was not a hearing in the Senate that I know of.

REPRESENTATIVE SCAVELLO: Passed fairly overwhelming.

MR. MCANENY: Yeah.

REPRESENTATIVE SCAVELLO: Thank you.

CHAIRMAN LEVDANSKY: Representative Kortz.

REPRESENTATIVE KORTZ: Thank you, Mr. Chairman.

Thank you, Mr. McAneny.

Under Senate Bill 961, it says you're allowed to increase the taxes five-tenths-of-one-percent. How much money would that help bring into Hazleton? And have you looked at it from the standpoint of funding the pensions and where would that lead to? You mentioned a place was --

MR. MCANENY: This does not cause a problem with the pension funding in any way because, as I said, this is really not a pension-funding bill. The -- and I'll be honest with you: I was involved in the drafting of the original legislation that you see before you, because there was another bill that attempted to amend Act 205 to expand the taxing authority under that statute, to which the commissions substantially objected.

This is not designed to be the imposition of a tax. It is a shift of a tax. Yes, it is limited to five-tenths-of-a-percent, which is the -- which would be more than sufficient to fund what Hazleton has been doing in the past, their overage, and the -- to pay that are OPEB requirements, their additional --

REPRESENTATIVE KORTZ: There is the healthcare portion.

MR. MCANENY: This is the healthcare portion, right. And this can only be assessed by a municipality that already is charging an Act 205 tax and it has to shift it from one tax to another. So from a taxpayer perspective, it's neutral. We're just shifting the authority for the taxes as opposed to creating a new financial burden.

REPRESENTATIVE SCAVELLO: Okay.

MR. MCANENY: I hope that answers the question.

REPRESENTATIVE SCAVELLO: It does, but there's a follow-up. Also on Senate Bill 961 they talk about it can be applied retroactively.

MR. MCANENY: Yes. That's to solve the -- aid the audit findings. The audit finding was done in 2003. Since it's not an imposition of a tax, I don't think retroactivity is a problem. It's just a shifting of statutory authority.

If this was an attempt to impose a tax going back to 2003 --

REPRESENTATIVE SCAVELLO: That's my concern.

MR. MCANENY: I would be the first to scream bloody blue murder, but I don't see it as an imposition because all they're doing is saying, "You've already imposed and collected the tax. You can change the authority going back." And all that does is clear up the paper finding with the Auditor General's office.

REPRESENTATIVE SCAVELLO: Thank you,

sir.

CHAIRMAN LEVDANSKY: Representative Nickol.

REPRESENTATIVE NICKOL: Thank you.

First, I wanted to explore a comment you just made about from a taxpayer perspective, this is neutral. If this legislation weren't passed, I gather that Hazleton couldn't levy the tax on residents working in the city who live outside the city; would that be correct?

MR. MCANENY: There is nothing in Act 205 right now -- this is an issue. There's nothing that indicates a right to tax nonresidents in the existing legislation. I don't --

REPRESENTATIVE NICKOL: It's kind of an issue over and apart from this.

MR. MCANENY: That is over and apart from it. And one of the things about moving it into the EIT tax -- which I know that's redundant, but that's what everybody says -- putting it in the EIT tax because there's never been an issue as to the earned income tax being imposed just upon residents.

We felt that that would solve that particular problem without having to address it directly.

REPRESENTATIVE NICKOL: But to the extent that we would move the tax base from being anyone who works in Hazleton plus Hazleton residents to just Hazleton residents, there could be -- I mean, some people would be paying less and some will be paying more by virtue of where they live, wouldn't they, to receive the same amount of revenue?

MR. MCANENY: That's true, but the question is: Where is the authority right now for the tax of the nonresidents? It's certainly not in Act 205.

So that's an iffy to begin with. It's one of those that we're trying to just have go away as a result of this.

REPRESENTATIVE NICKOL: Am I correct that Hazleton is bumping up against both limits on the way, the earned income and, in addition to that, on the property tax?

MR. MCANENY: It's my understanding that they have reached their maximum taxing authority under all available legislation.

The only other thing they could possibly do would be to apply for Act 47 distress, and I don't know that they have -- their financial situation is sufficient to justify that.

REPRESENTATIVE NICKOL: Do you, by any chance -- I know there have been some counties, municipalities more quickly bump up against the 12 mill property tax limits when assessments aren't done at a hundred percent of value or where reassessment haven't been made. Is that the situation in Luzerne County which handicapped Hazleton and puts them at that limit?

MR. MCANENY: I could not answer that question.

REPRESENTATIVE NICKOL: I think the mayor and others may be able to answer that.

MR. MCANENY: There are a number of others here that could answer that question.

REPRESENTATIVE NICKOL: I noticed in the comparison of Hazleton to other third-class cities, on page eight, that there is actually a slippage in the funding ratio. I noticed -- I just pulled out the fire plan over the period of time showing here and also in the nonuniform plan. I think the police plan is bouncing along with an increase, small increase, but why would we have seen -- with this additional revenue being generated for pension purposes, why would the funding ratio have dropped like that?

MR. MCANENY: I would imagine it's internal investment activity. As I said, there -- the money that they're collecting in this tax has not all been going into these pensions. If it were, we wouldn't be here, the Auditor General would not have cited them. It is because money collected under this tax is being used for nonpension purposes, which don't show up in this.

REPRESENTATIVE NICKOL: When you see 1999, a funded ratio of a hundred twenty-nine percent for the nonuniform plan, dropping down to 91 percent today, would that be the result of poor investment? Would that be the result of benefit increases, lack of funding or --

MR. MCANENY: Well, if I look --

REPRESENTATIVE NICKOL: It seems like things are going in the wrong direction, in other words.

MR. MCANENY: Yeah. That I really couldn't answer. It is entirely -- they dropped from a hundred ninety-nine -- the hundred ninety-nine funded is a -- is negative. That's not a positive. These are actuarial figures, and I apologize for that. So anything that looks positive is really negative, and anything that has a negative is really a positive.

These are references to the unfunded actuarial received liability, which you want to be in a negative funding -- a negative number status. So the best they have shown in their nonuniformed plan in 2001, they were at a hundred four, negative a hundred four, so they were overfunded at that point. They dropped to 50, negative 50 -- which, again, that's still a surplus -- in 2003. And we all know that that was not the world's greatest investment time frame.

And from there they went to a 23 in 2000, and to a 29 in 2007. I would imagine that those are based upon changes from investments more than anything else.

I -- nobody gets to keep track of

benefits structures in Pennsylvania. They don't have to report those to my agency. They only have to report the funding status. We get to see what the funding requirements are and to make sure the municipalities pay what's required in order to maintain the pension plans in accordance with Act 205. The Auditor General looks to make sure that the state aid is properly utilized.

But there is no agency at the state level that goes in and looks to say, "Well, you know, we think you shouldn't do a pension benefit increase," or "We don't like the way you're investing your pension." That's completely subject to local control.

REPRESENTATIVE NICKOL: One final question. Someone had told me earlier that this also applied to Altoona. Just wanted to make sure it did not. It was only Hazleton. I didn't know how broad it was.

MR. MCANENY: This bill will not apply to Altoona. And it cannot because of the population language, the census provision that was added in the Senate. That's what limits it to Hazleton only.

REPRESENTATIVE NICKOL: Okay. Thank you.

CHAIRMAN LEVDANSKY: Any other questions from members?

Mr. McAneny, I have a few questions.

When Hazleton's pension systems were first determined to be distressed, were they classified as at minimal, moderate, or severe distress?

MR. MCANENY: Moderate.

CHAIRMAN LEVDANSKY: Moderate.

MR. MCANENY: Yes. And that's because we don't classify them separately. We classify them as a total municipal package. You look at all three pension plans: police, fire, and nonuniform. And they were moderately severe.

CHAIRMAN LEVDANSKY: So there are three separate pension plans, but in the aggregate?

MR. MCANENY: Correct. The first -- the first requirement that every municipality must go into -- and this is not an optional provision under Act 205 -- is mandatory relief. You have to aggregate your pension plans.

Once you are distressed at any level, you must put together the aggregate pension system. So from that point on, everything is analyzed on the basis of aggregate.

So we aggregate the plans for purposes of determining distress, and the first thing they're required to do from that point on is to aggregate the plans for purposes of investment and administration. It reduces the administrative costs.

CHAIRMAN LEVDANSKY: Okay. Now, once it was determined that they were in moderate distress in the aggregate, what available remedies did Hazleton implement? Under Act 205, there are several -- there is an array of options available.

MR. MCANENY: That's correct. I do know that they did the aggregation of the funds. That's mandatory.

I don't believe -- well, the employer contributions did exceed the limits imposed by other laws. Third-class city code limits the amount of the employer contribution to the pension fund to be half of 1 percent of the revenues of the municipality other than that collected from debt. So they did exceed that one. So they did elect that.

I don't believe the employer contributions -- or the employee contributions exceeded the third-class city code.

I don't know if they did a revised benefit structure for newly hired employees. They only report a single pension fund to us. Normally when there's multiple pension structures, they'll list like two different plans, a police one and a police two or a fire one or a fire two. Here they just have one of each.

I don't know if they did the extended amortization periods. And I do know they did the tax.

CHAIRMAN LEVDANSKY: They did the tax. So of all the options, they chose to raise the wage tax. From what level to what level?

MR. MCANENY: If I recall correctly, they raised it by a half of a percent. So from one to one and a half.

CHAIRMAN LEVDANSKY: Is that because

they didn't want to tax nonresidents? They didn't want to deal with that issue?

MR. MCANENY: I don't have any ideas to the motivation other than they felt they needed the money to pay for these benefits and this was an available tax.

CHAIRMAN LEVDANSKY: So they have a variety of options available to them, but they elected to raise the wage tax.

Did they raise the -- did they -- are they at the cap at property?

MR. MCANENY: As I understand it, they are. They could not impose the Act 205 tax without being at the caps on both property and income. That's mandatory prerequisite.

CHAIRMAN LEVDANSKY: And they don't need court approval to raise the wage tax beyond the cap.

MR. MCANENY: Not under Act 205. They don't need court approval to impose a real estate tax beyond the cap either.

CHAIRMAN LEVDANSKY: As long as it's being used to fund retirement benefits.

MR. MCANENY: Well, as long as it's being used to meet the additional cost imposed by Act 205. Remember, this bill was passed at the end of '84. Prior to that, all pensions in Pennsylvania were funded on what they called a pay-as-you-go basis, which means nobody funded anything. You just paid the -- the municipality would pay the benefits due that year from that year's budget. They didn't have anything in a pension fund, for all intents and purposes. There was no money there other than what the state put in.

So Act 205 imposed this requirement that you pre-fund your benefits. The idea is that during the active employment life of the employee, you're going to collect into a fund the amount of money necessary to pay the pension benefits for that employee for the rest of their life. That's what entry-age normal is all about.

And Act 205 created this obligation that was a very, very substantial financial burden on a lot of municipalities. They hadn't had to pay anything like this before, so we had a bunch of different available methodologies to deal with that.

The original distress classification

under Act 205, nobody was interested. Nobody really was caring about these other methods of relief that were available. What they were caring about was that fact that they didn't get what they called supplemental state assistance, which was additional moneys appropriated by the General Assembly each year in addition to the money already being collected for general municipal pension system state aid. This was appropriated moneys that would then be paid out to just the distressed municipalities in various shares.

CHAIRMAN LEVDANSKY: And did Hazleton receive a supplemental pension assistance from the state?

MR. MCANENY: Oh, sure. During its early years, it did.

CHAIRMAN LEVDANSKY: And that expired in -- the authorization for the supplemental assistance expired in 2003.

MR. MCANENY: Yes. The end of 2003, the entire distress provisions, the supplemental state aid, the mechanism, in fact, by which we would be able to determine whether or not you're eligible for distress all expired the end of 2003.

CHAIRMAN LEVDANSKY: Now, the supplemental assistance answer that Hazleton received -- I'm flipping back through your testimony. On page five, you indicate the pension aid that Hazleton received from the state. Does that include the supplemental assistance?

MR. MCANENY: No. That's -- their supplemental assistance entitlement had already expired. Their funding status had risen to the point where they weren't getting any money under supplemental at that point.

CHAIRMAN LEVDANSKY: So they started out as -- they were first classified as -- their pension was first classified as moderate distressed. And what year was that determination made?

MR. MCANENY: 1987, if I recall.

CHAIRMAN LEVDANSKY: Okay. And then it went to minimal?

MR. MCANENY: Well, normally speaking -- this is one of the joys of the way Act 205 was drafted. There is no mechanism to change. Once you go in, you're classified at a certain distress level. The only mechanism to change that has to be triggered by the municipality itself.

That's why when I was saying that there were X number of municipalities that had originally been declared distressed, 52, and nine have since recovered, the declaration of recovery, the determination that they were now recovered from the distress classification was initiated by those municipalities, not by the commonwealth.

There is no mechanism in Act 205 to do an annual or whatever review of distress status and to re-determine that level.

CHAIRMAN LEVDANSKY: And those nine that kind of like self-classified themselves as no longer distressed, they lose the additional taxing authority available under Act 205?

MR. MCANENY: They lost the additional taxing authority. They lost the requirement that they aggregate their different funds for investment purposes. Whatever was available under Chapter 6 of Act 205, those additional remedies were lost to them at that point.

CHAIRMAN LEVDANSKY: So that the pension commission classified Hazleton as a moderate distressed pension system in 1987.

MR. MCANENY: Um-hum.

CHAIRMAN LEVDANSKY: And you're suggesting that that's never really changed; that it still remains classified as moderate --

MR. MCANENY: For all intents and purposes, everybody who has ever declared distressed is still declared distress with the exception of nine municipalities that have opted out.

CHAIRMAN LEVDANSKY: It's almost a vague sort of amendment to Act 205 rather than Act 511.

MR. MCANENY: Well, the trouble with Act 205 is this particular section, this whole issue dealing with the recovery status, is already gone. That expired in 2003.

We have, in fact, proposed legislation in the past, which we refer to as housekeeping, because we have this whole chapter of the act, which, for all intents and purposes, doesn't have a viability anymore. And if you're asking me, do I think there should be an Act 205 tax today? Probably not, because the whole purpose behind that was to cushion the shock of this new liability that the General Assembly imposed upon municipalities.

Well, that was, you know, 24 years ago. The shock has pretty well been cushioned by this time. We have proposed that sort of thing in the past, and it's just not gotten legs.

CHAIRMAN LEVDANSKY: If you could provide me later on with the amount of supplemental state assistance that Hazleton received, I'd appreciate that.

And just to clarify for me then, so they were first classified as moderately distressed, and they basically stayed that way because there is no mechanism in place to undeclare yourself?

MR. MCANENY: Well, there is a mechanism to undeclare yourself. There's just no mechanism to do it otherwise. I mean, Ambridge was declared distressed and it opted out. Now, anyone here familiar with the City of Ambridge?

I mean, there is a place that -- how do they opt out? How did they get out? But they are out. And it's just the way the statute was written that once the pension plan is not in trouble, you can, in fact, pull out.

A lot of these places don't need Act 205. They're already in distress, Act 47 distress. Act 47 distress gives them the ability right now to go to the court and get an increase.

In the home rule, there's no limit on their taxing authority. The home rule municipalities can tax without regard to Act 205. They don't need it.

There is a lot of other taxes that this works in conjunction with that.

Do we need Chapter 6 anymore? No.

CHAIRMAN LEVDANSKY: Mr. McAneny, a bit of a parallel here. I have -- one of the first municipalities ever declared financially distressed, pursuant to Act 47, is in my legislative district, and that was over 20 years ago.

MR. MCANENY: Right.

CHAIRMAN LEVDANSKY: And, to be honest with you, we had a meeting with them just a few weeks ago, and they seem as though they're very content to stay as financially distressed under Act 47, because they continue to want the extra taxing powers that Act 47 gains for them.

The parallel seems to be here that we pass Act 205, and we say that, you know, "Here's a range of options that you can use to deal with your pension plans and their financial status," and we give you these tools, and then you use one of the tools, which all too often is the easy route of simply raising local taxes, and you use that to pay for the pension fund obligations that you have. And then your pension fund is financially strong, you then use the money for something else.

I guess the question I have for you, wouldn't the other option be to reduce the wage tax that was imposed to fund the pension obligations rather than shifting it over to fund the post-employment benefits? That is an option, isn't it?

MR. MCANENY: It is, but certainly for the General Assembly to decide. I don't have -- my concern is that pensions are funded, and my concern initially with this bill is that I did not want to have language added to Act 205 that provided specifically for the use of this tax to fund OPEBs of any kind, because it creates tax issues and it was beyond the scope of Act 205, and I didn't want Act 205's scope broadened that far. It is not good for that account.

CHAIRMAN LEVDANSKY: One just final question, Mr. McAneny, for myself. The -- the ability for a pension plan to be declared minimum or moderate or severely distressed has expired.

MR. MCANENY: Yes.

CHAIRMAN LEVDANSKY: Okay?

MR. MCANENY: Correct.

CHAIRMAN LEVDANSKY: So why hasn't the ability to levy the tax to fund that problem, to address that problem, why hasn't the authorization to levy the tax expired concurrently as well?

MR. MCANENY: That is because of the way the legislation is written. It doesn't provide for that.

Chapter 6 had an automatic expiration date at the end of 2003, and what it says was going to expire were the provisions dealing with the designation of distress and the provision of supplemental state assistance. It didn't say anything about these other provisions expiring.

CHAIRMAN LEVDANSKY: Okay. That's enough questioning for me for now.

Mr. McAneny, with your expertise, I'd appreciate if you would attend the remainder of the committee meeting because we may have some follow-up questions that you could be helpful with.

MR. MCANENY: I will stay.

CHAIRMAN LEVDANSKY: Thank you very much for your testimony.

Mr. McAneny, could you step forward again. My executive director has a question he'd like to ask. Bob Kassoway, the executive director.

MR. KASSOWAY: The expiration language in the act states: The supplemental state assistance program and fund shall terminate in 2003 or in the first term which there are no municipalities entitled to receive supplemental state assistance, whichever occurs earlier.

MR. MCANENY: Right. So that took --

MR. KASSOWAY: Under Section 608, 608 is entitled Supplemental State Assistance Program and Fund. That paragraph in itself is the only reference to supplemental state assistance program fund, and that's which provides supplemental relief.

All the other language on the three categories of distress is elsewhere.

MR. MCANENY: Yeah.

MR. KASSOWAY: Why was it interpreted that they expired under that limited language that I just read?

MR. MCANENY: Because under the statutory construction act, we are not allowed to use the title of the section as controlling as to what it says, and that's the only thing that limits it.

If you look, there are provisions throughout that reference the fact that you have a distressed program and the fund, and the supplemental state assistance fund, so all aspects of the supplemental state assistance fund in the declaration of distress have been deemed to expire, but there's nothing that automatically expires the rest of it, because you can't use the chapter, the title heading on that subsection to control. We are supposed to pretend it's not there.

MR. KASSOWAY: Let me ask you, how did the process of determining that expired take place? Was it a request by the commission for a declaration? Did -- how was it determined?

MR. MCANENY: Well, the statute automatically -- you mean, how did we determine there was anything still left?

MR. KASSOWAY: That the expiration referred to more than Section 608 but that it referred to the entire section. I don't -- maybe if I go back and see what section -- Chapter 6, which established all these categories, is entitled Financial Distress

Municipal Pension System Recovery Program. And yet, the expiration language refers to simply the language under Section 608, which is entitled Supplemental State Assistance Program and Fund, and there again it says: The supplemental state assistance program and fund shall terminate in 2003.

MR. MCANENY: Which is what expired, the program and fund for supplemental state assistance. Not the distress classification provisions. There is two different things.

MR. KASSOWAY: I thought you said before they expired.

MR. MCANENY: No. No.

MR. KASSOWAY: I didn't understand what were you saying.

MR. MCANENY: No. What expired was the supplemental state assistance program, which is the method of designating such a thing, and the payment of the additional supplemental state assistance.

MR. KASSOWAY: See --

MR. MCANENY: Those moneys, they disappeared.

MR. KASSOWAY: I don't see where,

under Section 608, you have -- the method of designating occurs earlier.

MR. MCANENY: 607 is the provision that provides for these elements of relief, not 608. 607 is not the one that is entitled or addresses the supplemental state assistance program or fund.

MR. KASSOWAY: Just getting back to my original question, did the commission, through its interpretation, decide that the entire distress denotation expired because of this language, or was it ever an issue? Did anyone ever raise it as an issue?

MR. MCANENY: Yes, it was raised as an issue. In order to make a determination of distress classification, the commission required certain financial documentation, financial numbers from DCED, which actually, back then, when the bill was drafted, was DCA, but later became DCED, and those numbers were no longer available to us subsequent to 2003, so it was physically impossible for the commission to make a determination because the data was not collected by DCED any longer, and that was at the direction of the general counsel's office, as I understand it.

MR. KASSOWAY: Okay. So it was the administrative decision not to collect the data that was necessary to make a determination under the previous sections?

MR. MCANENY: It was an interpretation of the statute, and quite honestly, you know, since the bill only addresses the expiration --

MR. KASSOWAY: And that's not challenged by anybody?

MR. MCANENY: No, not to my knowledge. I know we had some questions about it, but they were resolved.

MR. KASSOWAY: Okay. Thank you.

CHAIRMAN LEVDANSKY: Thank you, Mr. McAneny.

Next, Mr. Martin Bergen, the director of the Bureau of Municipal Pension Audits with the Pennsylvania Department of Auditor General.

MR. BERGEN: Chairman Levdansky, Chairman Nickol, Honorable Members of the Finance Committee, good afternoon.

My name is Martin Bergen. I'm the

director of the Department of the Auditor General's Bureau of Municipal Pension Audits. Our bureau is responsible for auditing over 2500 municipal pension plans throughout the commonwealth. Our audits are conducted pursuant to the department's authority under Section 402(j) of the Municipal Pension Plan Funding Standard and Recovery Act, Act 205 of 1984, as amended, and in accordance with Government Auditing Standard issued by the Comptroller General of the United States.

The objective of our audits is to determine if pension plans have been administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies.

I'm pleased to represent the Department of the Auditor General today at today's hearing on Senate Bill 961 of the 2007-08 legislative session.

I wish to emphasize at the outset of my remarks that due to the department's role as an independent audit agency, I am not here today to opine as to the merits of the proposed legislation. Instead, I intend to provide an analysis as to what effect the legislation would have on the department's recent audit of City of Hazleton's unauthorized usage of the proceeds from a special municipal pension tax levied by the city under the authority of Act 205.

On August 3rd, 2006, the department released the report of an audit that it had conducted of the City of Hazleton's aggregate pension fund. A copy of finding number one of the audit report is attached to my testimony.

Finding number one cited the city for an improper expenditure of special municipality tax proceeds. Pursuant to authority granted by Section 607(f) of Act 205, the City of Hazleton levies a special municipality tax of four-tenths-of-one-percent on earned income and net profits to be used exclusively for funding the city's pension plans.

Section 607(f) states that, quote, The proceeds of this special municipal tax increase shall be used solely to defray the additional costs required to be paid pursuant to Act 205, which are directly related to the pension plans of the municipalities.

However, our audit found that during the years 2003, 2004, and 2005, the city improperly used, from this special municipal tax, in the total amount of $1,426,656 to fund post-retirement healthcare benefits for police officers and firefighters who retired after January 1st, 1999. Prior to 2003, those expenses were paid through the city's general fund.

In addition, the city used $166,466 of special municipal tax proceeds in 2003 to buy back unused sick -- unused vacation and sick leave from employees who accepted an early-retirement incentive offered by the city.

As a result of the improper expenditure of special municipal tax proceeds for post-retirement healthcare benefits and unused leave buy-backs, the funds were not available to paid authorized pension plan expenses or for investment purposes in accordance with Act 205.

Our audit report contained a

recommendation that the city either reimburse the Act 205 special municipal tax account for the $1,593,122 of improper expenditures or deposit that amount into an eligible pension plan.

We further recommended that the city discontinue paying for post-retirement healthcare benefits with special municipal tax proceeds or assets of aggregate pension fund. The city disagreed with our finding and recommendation.

The department has the legal authority to enforce the pension audit finding through the department's responsibility under Act 205 for distributing annual state pension aid from the commonwealth. Accordingly, due to the city's noncompliance with our recommendation, the department subsequently issued an Order to Show Cause, pursuant to which the department will withhold the city's allocation of state pension aid for calendar year 2007 and all future years unless and until the city complies with the report's recommendations.

The city requested an administrative

hearing within the department governed by the general rules of administrative practice and procedure; however, the parties have agreed to continue the administrative hearing in order to allow time for a mutually satisfactory resolution of all or part of the dispute, including, but not limited to, the passage of the legislation we are discussing today.

Because the administrative hearing has not yet occurred, the parties agreed last year that the department would distribute the city's 2007 state pension aid. The parties are in the process of finalizing a similar agreement regarding the 2008 aid.

Based on the department's analysis of the current version of Senate Bill 961, Printer's Number 1168, and after consulting with staff from the Public Employee Retirement Commission, if enacted into law, Senate Bill 961 would resolve finding number one with regard to past and improper use of special municipal tax proceeds. In other words, the city would no longer be required to comply with our recommendation to either reimburse the Act 205 special municipal tax account for the $1,593,122 of improper expenditures or deposit that amount into an eligible pension plan.

If the city has continued to make improper expenditures of special municipal tax proceeds since 2005, we would expect this figure would be significantly larger, and we would have to continue to issue findings and recommendations in future reports similar to finding number one.

It is important to recognize that Senate Bill 961 merely amends the Local Tax Enabling Act, Act 511 of 1965, as amended, in order to provide retroactive legal authority for the city to have collected the taxes to fund the benefits at issue. The legislation does not and should not amend Act 205.

Therefore, the city and other municipalities would still be prohibited from using special municipal pension tax proceeds to fund post-retirement healthcare benefits or vacation or sick leave buy-backs. We would have to review any actual or proposed changes to the current version of the legislation to determine their effect on this analysis.

Thank you for the opportunity to present this testimony on behalf of the department of the Auditor General. Attached to my testimony is a summary of prior audit reports containing findings pertaining to unauthorized uses of Act 205 special municipal tax proceeds and the subsequent disposition of those findings.

I would be happy to answer any questions.

CHAIRMAN LEVDANSKY: Thank you Mr. Bergen.

Any questions from any of the members?

Representative Kortz.

REPRESENTATIVE KORTZ: Thank you, Mr. Chairman.

Thank you, Mr. Bergen, for your testimony.

The auditing that you've done, other than Hazleton, how many other cities have you found that have done the same thing?

MR. BERGEN: Hazleton is the only audit report where the funds from the special tax proceeds have been used to fund post-retirement healthcare benefits.

We have done a couple audit reports where municipalities have used those tax proceeds to fund general fund expenditures, but this is the only one related to the post-retirement healthcare benefits.

REPRESENTATIVE KORTZ: Okay. And the reason I'm asking that question, Senate Bill 961 really restricts it to Hazleton. I'm wondering if we shouldn't expand this because you may find, as you go through the state, there's other cities in the same problem.

MR. BERGEN: We typically audit third-class cities every two years, and as I just indicated, so far Hazleton is the only one that we've come across this issue.

REPRESENTATIVE KORTZ: Okay. Thank you.

CHAIRMAN LEVDANSKY: Representative Scavello.

REPRESENTATIVE SCAVELLO: Thank you, Mr. Chairman.

And thank you, Mr. Bergen, for your testimony.

You made a comment. If 961 passes,

it doesn't address what's happening now in Hazleton. Is that what you're saying? I'm reading: The legislation does not and should not amend Act 205 for the city and other municipalities would still be prohibited from using special municipal pension tax proceeds.

So they wouldn't be able to continue to do what they're doing; is that what you're saying?

MR. BERGEN: If Senate Bill 961 passes, it wouldn't affect -- Act 205 is not being amended by this legislation.

REPRESENTATIVE SCAVELLO: Correct.

MR. BERGEN: So no municipalities would be allowed to use the Act 205 tax to pay their post-retirement healthcare benefits. Hazleton would, in effect, be getting a tax shift that would be applied retroactively to 2003, pursuant to this legislation.

So the point I was trying to make was that this wouldn't affect our audit procedures in reviewing that special tax proceeds were only used to defray pension cost.

REPRESENTATIVE SCAVELLO: You mentioned some municipalities have taken that money and put it in the general fund, which, to me, would seem a lot harsher than, here, we're still taking care of the police and -- the police department, you're taking care of the fire folks. It's related in some way. It is not pension, but it's related in some way. I would think that would be a gross negligence in my estimation

MR. BERGEN: Correct. And we've encountered only a couple of those instances, and in those cases they had to reimburse the pension fund for the amount that they previously diverted from the pension fund.

REPRESENTATIVE SCAVELLO: Now, for municipalities such as Hazleton -- I know the chairman mentioned it earlier -- if this doesn't happen, if we can't help them with this, they're going to have to raise the tax and other tax in order to do it; am I correct? Moneys have to come from somewhere. Somebody has to pay for it.

Those benefits, those employees are -- those benefits are due to employees, so if it's not from this tax, they have to raise the property tax or something else.

MR. BERGEN: I would presume so. Obviously, I'm sure the mayor could address that situation, but I would presume so.

REPRESENTATIVE SCAVELLO: Okay. Thank you very much.

CHAIRMAN LEVDANSKY: Representative Nickol -- I'm sorry. Representative Vulakovich.

REPRESENTATIVE VULAKOVICH: The other ones that put the money into the general funds, so to speak, they've all paid the money back?

MR. BERGEN: Correct.

REPRESENTATIVE VULAKOVICH: So the only one out there is Hazleton that has a money issue where they have to pay money back?

MR. BERGEN: Correct.

REPRESENTATIVE VULAKOVICH: Out of all 2,000 some?

MR. BERGEN: Well, only approximately -- Mr. McAneny had the figures in his testimony. I believe it's about a dozen municipalities collect the special tax. It's not the 2500 throughout the commonwealth.

You can only collect the special tax

pursuant to what he had previously outlined.

REPRESENTATIVE VULAKOVICH: So if we pass this, then they don't have to pay the money back. That's a cease and desist, and they can do what they're doing now.

MR. BERGEN: Correct. It is, in a sense, a tax shift.

REPRESENTATIVE VULAKOVICH: So do we open up a can of worms for some other municipalities coming and looking at this and saying, "Why can't we start" -- if we are amending 511 taxes, we're going to amend 511 specially for Hazleton. No other municipalities.

MR. BERGEN: That's my understanding of this particular bill.

REPRESENTATIVE VULAKOVICH: So other municipalities, say of the third-class city to come and say, "Why can't we do this now under 511?" Why are we -- why just Hazleton?

In other words, we're trying to solve their problem, and I sympathize with it. Act 205 and Act 600 -- Act 600 is a real problem.

Can we do this?

MR. BERGEN: Obviously what would

happen down the road is speculative. I mean, my intention today obviously was to present the department's interpretation of the bill as it pertained to the audit report, and what would come down the road is speculative.

REPRESENTATIVE VULAKOVICH: I mean, there is no other way of helping them with this situation other than legislation of this nature?

MR. BERGEN: At this point, I would presume so.

REPRESENTATIVE VULAKOVICH: Okay. Thank you.

CHAIRMAN LEVDANSKY: Representative Nickol.

REPRESENTATIVE NICKOL: I'm curious. You talked about the early-retirement incentive in 2003. I look at the payroll figures for all three categories of employment, and usually you grant an early retirement system to reduce payroll costs. And it appears that the police costs fell considerably, but the other two, the payroll continued to grow.

Do you know, was this early-retirement incentive only for the police, or did it extend to other employees within Hazleton?

MR. BERGEN: I believe it was for police and firefighters.

REPRESENTATIVE NICKOL: Okay. Thank you.

CHAIRMAN LEVDANSKY: Director Kassoway.

MR. KASSOWAY: You mentioned that -- you mentioned that you cited them for the fact that they used it for the healthcare benefits which were previously funded from the general fund.

Were they funded by the general fund by putting general fund money into the pension system and paying for it, or were they just --

MR. BERGEN: This is totally outside the pension plan.

MR. KASSOWAY: They were outside the pension. The previous gentleman mentioned a court case out in Pittsburgh that they -- the Court said that you should consider those health benefits as part of the pension system.

Then I would think they would run into a different problem. Because if you considered the health benefits as part of the pension system, and you were previously paying for those benefits out of the general fund, then you'd run in violation of the authority for the special tax that says it can't be placed in the general fund money, because then you'd be replacing the general fund money that would be paying for the healthcare benefits and you'd be run afoul of the law there.

One last question. You cited them for doing this in '03, '04, '05.

MR. BERGEN: Correct.

MR. KASSOWAY: You've been doing audits since the act went into effect, I imagine, in the mid '80s?

MR. BERGEN: Correct.

MR. KASSOWAY: So are you saying that '03, '04, '05 was the first time they used the money outside of the authorization?

MR. BERGEN: Correct.

MR. KASSOWAY: So the misuse of the money began in '03, '04, and '05, according to your audit?

MR. BERGEN: Yes.

MR. KASSOWAY: Thank you.

CHAIRMAN LEVDANSKY: As a follow-up to that, and you issued -- your audit was done in, I guess, '05, and your report was finalized at the beginning of '06.

MR. BERGEN: Yes.

CHAIRMAN LEVDANSKY: And you recommended that the city discontinue paying for the post-retirement healthcare benefits with this special tax. You made that recommendation back in '05, beginning of '06.

MR. BERGEN: Yes.

CHAIRMAN LEVDANSKY: Has that recommendation been implemented?

MR. BERGEN: We are currently doing a follow-up of the city's pension fund audit report for the years '05 and '06. The prior audit report was for '03 and '04, although we commented on issues that were occurring in 2005.

That report has not been released yet. I'm not at liberty to comment on the particulars of that report. I did indicate in the testimony that, you know, should the situation continue, and absent the passage of the legislation, we would certainly expect the figure to increase from the prior audit report.

CHAIRMAN LEVDANSKY: And I think Mr. McAneny mentioned earlier that there -- as I recall, 52 municipalities were deemed to have some level of distressed pension pursuant to Act 205. Eleven availed themselves of the option to raise taxes to fund their pension obligations.

Has the department audited all 11 of those, including Hazleton, the other ten?

MR. BERGEN: Yes.

CHAIRMAN LEVDANSKY: And just so that I'm clear on this, and of those ten, what did the audit findings reveal relative to those ten and their use of this special tax provision?

MR. BERGEN: Well, we've been conducting audits, as I previously indicated, even prior to the advent of Act 205, which was in the mid '80s, but obviously with the third-class city, the department has been doing audits of the third-class cities for many years.

As I indicated, that we have found a couple instances in cities where there was a misapplication of the Act 205 tax funds. I believe we had three other reports that we were able to find that had findings of that nature.

CHAIRMAN LEVDANSKY: And what was the -- so of the ten, outside of Hazleton, that had misused these funds for purposes not authorized under Act 205 -- three of the ten, of those three, what -- and in terms of follow-up, did they take corrective action? Did they pay back or --

MR. BERGEN: Yes.

CHAIRMAN LEVDANSKY: They did?

MR. BERGEN: Yes.

CHAIRMAN LEVDANSKY: Okay. So three of the ten are not in compliance with the law -- I'm sorry -- four of the eleven are not in compliance with the law. Three, then, take action to come into compliance. And this legislation -- this legislation would enable one of them, one of the eleven, to essentially get a benefit under the law that nobody else has. How would you react to that?

MR. BERGEN: Well, again, I'm not prepared today to opine the merits of the bill. I strictly am speaking to its relevance pertaining to the audit finding.

CHAIRMAN LEVDANSKY: You mentioned the '03 -- the audits were done in '03, '04, '05. How much total funds must be paid back?

MR. BERGEN: I believe the total was 1,593,122 was cited in the audit report that was released.

CHAIRMAN LEVDANSKY: And how does that compare with the other three municipalities that were out of compliance with the provisions of Act 205?

MR. BERGEN: I believe that there was an instance of -- with the City of Altoona, that was an audit that was 2.2 -- $2,277,187.

We just released an audit report of the City of Aliquippa with a hundred fifty-one thousand, two hundred sixty-one dollars.

CHAIRMAN LEVDANSKY: And what was the third municipality?

MR. BERGEN: The third municipality was the City of Butler.

CHAIRMAN LEVDANSKY: And how much?

MR. BERGEN: The City of Butler had -- their finding dealt with timing issues that the report was -- excuse me -- the tax funds were being used -- were not being deposited timely into the pension funds, and then they were -- eventually they were all placed into the pension funds.

There was another issue that they had. There was a dispute in the city that the police officers -- regarding police officers' contributions that were past due, that went to arbitration, and the city, in collective bargaining -- in collective bargaining, agreed to pay that hundred seven thousand for past-due police contributions to the pension fund.

CHAIRMAN LEVDANSKY: Now, back to Hazleton. So the 1.5 million in the aggregate for all three years total?

MR. BERGEN: Yes.

CHAIRMAN LEVDANSKY: Roughly.

MR. BERGEN: Yes.

CHAIRMAN LEVDANSKY: And that 2.2 million for Altoona, that was the aggregate that occurred over a period of years as well?

MR. BERGEN: The audit report was from 2002 to 2003.

CHAIRMAN LEVDANSKY: That's a two-year. And what -- what happened with Altoona when you discovered that they had misapplied the use of these funds as well to the tune of 2.2 million? How did they handle that?

MR. BERGEN: The city reimbursed $2,616,976 to the special municipal tax fund account.

CHAIRMAN LEVDANSKY: And what year did they do that, do you know?

MR. BERGEN: It was subsequent to our audit period. I don't have the exact date. I would speculate that it would be 2004, 2005.

CHAIRMAN LEVDANSKY: Okay. Okay. One final question. Given that Hazleton is not in compliance with the requirements of Act 205, what funding -- is there any state funding subject to withholding because of Hazleton's noncompliance with Act 205 provision?

MR. BERGEN: The regular state pension allocation -- the audit report did contain a potential withhold of their state aid allocation. Now, we have continued that. We have -- we gave them their 2007 allocation, and, you know, we're working on an agreement to assist them with their 2008 allocation. But the department has the right to withhold the allocations in the future.

CHAIRMAN LEVDANSKY: Okay. One final question as follow-up from my executive director, just to keep it clear in my mind: The state allocation that you speak of, is that considered general fund money by the municipality, or is that outside?

MR. BERGEN: The state aid comes from the commonwealth, and it must be deposited into the pension plans.

CHAIRMAN LEVDANSKY: Okay. So when the act talks about not reducing any general fund -- contribution to the pension fund, that's general fund money that they raise locally versus any money they might get through the state through these allocations, or not?

MR. BERGEN: I'm not quite sure I --

CHAIRMAN LEVDANSKY: I'm just trying

to -- the money that they get -- and they get that from, what, the fire and casualty, the fire and car insurance proceeds that are directed to -- by formula to them?

MR. BERGEN: Yes.

CHAIRMAN LEVDANSKY: Does that -- is that considered general fund money when it's taken by the municipality and put into a pension fund, or when the act talks about general fund -- municipal general fund moneys, are they talking about moneys raised locally through taxes or something else?

I'm just trying to find if there is a distinction between the two. Maybe I'll ask Hazleton when they get up.

MR. BERGEN: I mean, clearly the state aid funding is not considered general fund money. It's just strictly allocations from the commonwealth to be deposited into the pension plans.

CHAIRMAN LEVDANSKY: Okay. Thank you.

Mr. Bergen, thank you very much for your testimony --

MR. BERGEN: You're welcome.

CHAIRMAN LEVDANSKY: -- your insight.

I'm sorry. Representative Brian Ellis.

REPRESENTATIVE ELLIS: Thank you, Mr. Chairman.

I'm sorry to have not asked this sooner, but I've been listening here and I'm just a little bit confused about a couple things. Certainly representing the City of Butler, I know what we went through.

How long did it take us to actually get into compliance in the City of Butler?

MR. BERGEN: Well, the compliance with the audit recommendation was noted in the follow-up audit, and they're usually done every two years for third-class cities.

REPRESENTATIVE ELLIS: Now, hypothetically, if Butler would have said -- called the department and said, "I'd like to have an appeal," then naturally they would have not got into compliance until after the appeal; is that correct?

MR. BERGEN: I would assume so, yes.

REPRESENTATIVE ELLIS: So that's essentially what we're looking at right here.

The City of Hazleton has not said, "We are not going to paid it. We don't -- we just think we have a difference of opinion right now. Let's wait and let's have a hearing, and when we find out, we'll be happy to pay it if we have to." In the meantime, if the law got changed, the law got changed.

Is that the simple version of what's going on here?

MR. BERGEN: Well, the department is in a process of resolving the matter with the city, and there have been ongoing discussions with representatives of the city, and, you know, one of the potential resolutions to the situation is the proposed legislation, and so I guess this is part of the process.

REPRESENTATIVE ELLIS: And, Mr. Bergen, you said that the follow-up reports come out when, in mid October or you didn't say?

MR. BERGEN: It hasn't been released yet. I would expect this fall.

REPRESENTATIVE ELLIS: Okay. Thank you very much.

CHAIRMAN LEVDANSKY: Representative

Vulakovich.

REPRESENTATIVE VULAKOVICH: In that report, when did -- what is the MMO going to show? That they owe -- that the township or the municipality has to pay -- their contribution is 1.5 plus whatever?

MR. BERGEN: This is separate and apart from the MMO.

REPRESENTATIVE VULAKOVICH: So the MMO would tell them what they have to do on a normal basis?

MR. BERGEN: Yes. The MMO is their normal minimal funding requirement.

REPRESENTATIVE VULAKOVICH: And then 1.5 would be additional -- would be additional --

MR. BERGEN: That would be additional, yes, to the MMO. Yes.

REPRESENTATIVE VULAKOVICH: Thank you.

CHAIRMAN LEVDANSKY: Representative Scavello.

REPRESENTATIVE SCAVELLO: Thank you, Mr. Chairman.

I keep hearing, you know, that the

City of Hazleton is looking for something special that we do not allow -- we would not allow anyone else, but in the last term, just for the record, we did pass two pieces of legislation, one for Harrisburg and one for Philadelphia, allowing them special taxing powers in those two cities.

With the assistance -- and I know at those hearings there was representation from those two cities in support of those taxing powers that has to do with room tax in both of those two cities. I see you have a representative there from that area, and I know that the senator from that area also supports it.

So I just want that as part of the record, because we have in the past allowed municipalities from -- other cities and municipalities those special privileges. We can also go back to the sales tax in Philadelphia and Pittsburgh where we allowed them to raise their sales tax by 1 percent more than the rest of the state as well.

Thank you.

CHAIRMAN LEVDANSKY: Yes, and just

for the record as well, when we give special tax authorization to a municipality, we state the purpose for it. And Allegheny County was to fund the RAD, the Regional Assets District, and that's what it funds. It can't be used to fund something else.

And when the legislature just recently gave special additional tax authorization to Philadelphia to raise the hotel tax, that is used to fund their convention center expansion and their visitor's bureau. It can't be used to fund the debt of employees -- I'm sorry, or the pension obligation for the employees or the post-employment benefit program of employees.

So while we do give special taxing authority to municipalities, we always state what that tax authorization is to be utilized for.

Another's follow-up by Chairman Nickol.

REPRESENTATIVE NICKOL: Thank you.

One thing that troubles me in looking at one of the charts presented by Mr. McAneny about Hazleton's funding is -- I understand with regard to fund ratios, if you show progress in terms of fully funding your retirement benefits, your ratio goes up over time.

And we have a chart here that goes from 1985 to present, and just looking at that period of time, Hazleton made tremendous progress in terms of its fund ratio through the reports in 2001. And then -- and I can understand between 2001 and 2003, we took a market tumble, but 2003 to 2005 and to 2007, the funded ratio deteriorated in -- in one of these periods it's all three of their funds, and in the other period in two of the funds.

Does the Auditor General look at things like that? I mean, it appears to me, you know, from what I'm hearing, is the money that perhaps should have gone into those funds was used for another purpose, and at the same time, I mean, if the fund ratio had continued, maybe we might not question, but it appears that the funding ratio has actually dropped since they started using the money for the other purpose.

Does the Auditor General look at that

and comment on the funding ratio and the progress in terms of having enough money to pay benefits?

MR. BERGEN: There was an issue with the city's pension fund years ago -- I don't recall the specific year; it was a few audits ago -- where the city did provide some pension benefit enhancements. I believe it was to the police officer and the firefighters. I'm not sure exactly if it was for both, but -- and I think the cost of those benefit enhancements, which were cited in our audit reports, are probably reflected in those funding figures.

And the city was cited for providing benefits in excess of a third-class city code, and they have taken steps to address our prior audit findings.

REPRESENTATIVE NICKOL: Thank you.

CHAIRMAN LEVDANSKY: Mr. Bergen, again, thank you for your testimony and your insight.

Next, I'd like to call the panel -- two-person panel, Mark Koch, the legislative chairman and the immediate past president of the state Fraternal Order of Police, and

Mr. Sean Welby, legal counsel for the Pennsylvania Fraternal Order of Police.

Welcome.

MR. KOCH: Thank you very much, Mr. Chairman and the committee, for allowing us this opportunity to appear before you today. Just like you, we also are very concerned with the pension issues surrounding our uniformed services. Obviously, it is a very, very important issue that the men and women that have served be provided adequately and be protected with their pensions.

However, in the interest of time today, our written testimony that I've prepared, and I'm sure you have many questions. I do have our legislative counsel, so if you don't mind, I'll have him read the testimony. Thank you.

MR. WELBY: Actually, thank you, Mr. Chairman, and in deference to Mr. Koch and the time, I notice that we've gone a little bit over our allotted time. I was hoping, therefore, with your permission, to depart from my written comments and address this issue as succinctly as I possibly can.

The issue as we see it is not whether the City of Hazleton misused its taxing authority under Act 205 for inappropriate purposes. Clearly, the city, in good faith, did everything it could to fund its benefits structures in a way that it felt was in accordance with the act.

If the Auditor General, in fact, found that to be not the case, then that is an issue to be dealt with between the parties there.

The issue here today is what are we going to do going forward with respect to the taxing authority under Act 205 and the ability to use that enhanced taxing authority to substitute another revenue-raising capability that other municipalities don't have right now.

In these dire financial times, we at the Fraternal Order of Police is not going to take the position that a municipality, any municipality, should be hemmed in in its ability to raise tax revenue from any source. These are situations that these municipalities find themselves at, basically through economic conditions that are trickle-down from the national economy to the state to the local levels, and they cannot control it.

However, the legislation in front of you does raise some issues with respect to the interest of the Fraternal Order of Police that we hope the committee can address and find satisfactory answers with so that they can work with the city to avoid any potential financial crisis.

I believe it was Representative Scavello who said at least they are taking this money, and if they weren't using it for the purposes that the statute required, i.e., funding their Act 205 liability under their statutory obligation, well, at least they were taking that money and utilizing it for the purpose and benefit of employees. They were funding post-retirement healthcare insurance with that money.

That, in fact, based upon the outcome of the audit, seems to be the case. However, as drafted, Senate Bill 691 -- 961 does not limit the expenditure of this additional taxing authority or substituting taxing authority to any particular purpose.

As the chairman pointed out, when the General Assembly authorizes a departure from the statutory caps or statutory maximum for taxes, there's a purpose set forth. Whether that purpose is a good purpose or a bad purpose, is a worthy purpose or not, is a decision for the committee of the General Assembly to make in their wisdom.

In this particular case, the funding of post-retirement healthcare benefits or buy-out benefits or any other benefits may be based upon your value system or the interest of your constituents and worthy and appropriate cause. However, this legislation does not limit the proceeds of that additional taxing authority to that or any issue.

The chairman says when Act 47 municipalities become involved in Act 47, sometimes it seems like they don't want to get out. And that has been the experience of the Fraternal Order of Police as well, because of the enormous ability to raise revenue. We sometimes refer to it as municipal crack cocaine. That municipalities have this authority. They don't have to listen to anyone in order to be able to raise this revenue, and also spend the revenue in any way that they so choose.

The problem as we see it and what we hope for as an answer with respect to the deliberations that takes place with respect to this legislation is that if there is going to be a substituted authority to raise additional revenues above the caps that we have, that there are be a dedicated purpose associated with that.

Otherwise, what happens is the same thing that happens when you have a pot of money in the General Assembly. That pot of money becomes subject to political considerations. It can become subject to appropriation for whatever political consideration is top of the agenda at the moment.

There is no question, all employers are facing increased liability because of GASB 45 and its requirement that municipalities account for accrued but unfunded for future expenses. No question about it.

However, if we are going to take action and, as some would have it, grant a special taxing authority or substitute a special taxing authority for the City of Hazleton, isn't it appropriate that we do so so that we are addressing the true issue at hand, not placing the money into the hands of future administrations that are going to be subject to political pressure as to how to spend it.

Whatever the wisdom of the city in complying with or allegedly not complying with Act 205, the city has done its best in a good faith effort to fund employee benefits that it did not agree to. The employee benefits at issue go back prior to 1985.

Post-retirement healthcare benefits first were a policy within the City of Hazleton prior to 1985. Those benefits were limited and a restriction put on them by an Act 111 arbitrator in 1985. And since then, there have been at least three occasions -- 1986, 1997, and 1999 -- that the parties agreed to modify those post-retirement benefits even further voluntarily outside the -- outside the arbitration process voluntarily through collective bargaining in an attempt to address the growing unfunded liability.

The parties have attempted to address this issue in a lot of different ways, and it's not just a question of coming up with a tax. What our concern is and what our hope is that the city can give us today in its testimony is some kind of assurance that if we are going to recognize the need and the righteousness of this cause, that those funds so raised be specifically appropriated for a particular purpose.

And that, in accordance with what the chairman had pointed out, has been the history of the General Assembly in this regard.

With that, gentlemen, I will take any questions you might have.

CHAIRMAN LEVDANSKY. Thank you, Mr. Welby.

Any questions from the members?

Mr. Welby, I don't have a question, Mr. Koch, as much as a comment. You're correct in terms of my concern is that if municipalities -- if the legislature chooses to authorize this, then it ought to be authorized for other municipalities that are similarly situated in terms of their pension funds.

Hazleton is by no means unique amongst municipal pension plans. There are other municipalities with equal or more pressing pension obligations. And if it's the decision of the legislature that we ought to permit this extra -- this authorization, this extra tax be used, it ought to be for a purpose and ought to be for a purpose for other similarly situated municipalities as well.

But that's largely what my concerns are. But I appreciate that -- your deviation from your prepared testimony. And I appreciate your testimony as well.

MR. WELBY: Thank you, Mr. Chairman.

MR. KOCH: Thank you very much.

CHAIRMAN LEVDANSKY: My executive director has a question.

MR. KASSOWAY: Maybe with your familiarity with other cities, do other taxing jurisdictions generally pay for their health benefits, retired health benefits through their pension contributions or through their general fund?

MR. WELBY: That has -- under the law, the pension plan -- no pension plan benefits may ever be utilized to provide any other benefit but a pension retirement benefit. All municipalities in Pennsylvania that provide for post-retirement healthcare or any other post-retirement benefit, including the commonwealth, that does serve through general fund moneys.

Now, since the advent of GASB 45, which is the new accounting standard which now is going to require governmental agencies and entities to account for such unfunded liabilities, there has been talk, and it has been thus far simply talk, of municipalities creating certain sinking funds to address these potential unfunded liabilities by putting in special accounts where we're going to fund for these in advance the same way we do pensions.

Unfortunately or fortunately, however

you want to take a look at it, I had just had an opportunity to have an interaction with one of the top municipal pension actuaries in the commonwealth who has over a hundred municipal pension clients, and basically is the management actuary.

I had asked him whether, in fact, people were starting to create sinking funds on a regular basis, sort of like a separate pension fund to fund these benefits, and out of the hundred municipalities that he represents, three have done so.

As a matter of fact, the commonwealth itself operates on a pay-as-you-go nature with respect to post-retirement healthcare. The Pennsylvania healthcare benefits, the members of the committee and their staff, based upon their service today, is not going to be paid for today; it's going to be paid for in the future. And it's going to be paid for largely on a pay-as-you-go basis.

MR. KASSOWAY: What percentage of municipalities taxing jurisdiction would you say provide post-retirement healthcare benefits?

MR. WELBY: Well, with respect to municipalities employing a police department, which would be my area of expertise, there is approximately 900 municipal police agencies within the commonwealth. Of those 900, with respect to third-class cities, what we're here for today, the vast majority, if not all of them, provide for post-retirement healthcare.

MR. KASSOWAY: So they had to make the tough decision to provide for those expenditures versus some other municipal service that they might provide. Would your organization support this legislation if we gave the authority of a set percentage increase for earned income tax to provide for this very purpose for all the taxing jurisdictions?

MR. WELBY: I would have to defer to Mr. Koch on that.

MR. KOCH: Yes, I'm sure that's primarily the issue that we have or the concern that we have. We are not opposed to this legislation. But that's a question that we do have. And I'm sure that, again, number one thing, just as you, I agree with you and

Mr. Chairman and everyone here, the concern's the protection, of course, of those that have served, and how should we reach that goal at the same time with the problems we are facing.

So I'm sure that would be -- that would be very positive.

CHAIRMAN LEVDANSKY: Thank you.

MR. KASSOWAY: Thank you.

Mr. Koch, Mr. Welby, thank you very much for your testimony and your insight. Appreciate it.

MR. KOCH: Thank you very much.

CHAIRMAN LEVDANSKY: We're running a little bit late, but I appreciate the mayor and his people from Hazleton being here. I'd like to call them up here to the panel. Mr. Richard Miler, and Mr. Christopher Gabriel, both attorneys with the law firm of Campbell, Durrant, and Beatty, and the mayor of the City of Hazleton, Mayor Lou Barletta.

MAYOR BARLETTA: Good afternoon.

MR. MILLER: Please the Chairman, I'm Rich Miller.

MR. GABRIEL: I'm Christopher

Gabriel.

MAYOR BARLETTA: I'm Mayor Lou Barletta.

MR. MILLER: Representative Levdansky, we have prepared a written statement and much -- as stated in the comment on the state FOP, because of the time crunch, we're prepared not to read through that official written statement.

I think the mayor has a few opening comments he'd like to make followed by a few points regarding the legislation in this process that I'd like to make. At that point, we'd be pleased to answer questions.

MAYOR BARLETTA: Thank you.

First of all, I'd just like to thank --

CHAIRMAN LEVDANSKY: One second, Mayor. I'd welcome the mayor to give some opening comments and say whatever he says, but I'd appreciate it if -- Mr. Miller, if you'd just proceed with your regular testimony. It's very specific and I think will be very instructive.

Mayor Barletta.

MAYOR BARLETTA: Thank you. I'd like to thank the committee for taking the time to address this very critical issue that we face right now.

You know, I'm here not only representing myself; I'm here without objection to this bill. City counsel is here with us, members of the police department, fire department as well. We have a letter with no objection from the Auditor General's office as well as PERC. And coming in here with a bill that passed the Senate 49 nothing.

I've heard a lot of comment today, some favorable, some unfavorable. If I may just, as a mayor, I'm sure it would be nothing new to anyone here to hear how difficult it is today to provide services to the citizens that we represent.

It is becoming more and more difficult with the rising cost of healthcare, with the rise of crime, and our most important, I believe, obligation is to protect the people that we represent, and we have opted, when I became mayor in the year 2000, not to go Act 47, which many cities have.

We decided to make very difficult decisions and be responsible financially to get the city back on its feet, which other cities may not have chosen that route. And we have, to the credit of the unions that work together with this administration and the employees and the citizens of Hazleton.

We have come to this point where this bill, at the end of the day, with all its pros and cons, doesn't hurt anybody, but actually helps the city from becoming Act 47, which will hurt someone. It will hurt our employees. It will hurt the citizens of Hazleton. This does not affect our pension.

It is just a common-sense way that I believe cities need to look at going forward so that we can continue to protect the citizens that we represent.

So with that being said, I would like to thank you for taking this time.

MR. MILLER: Chairman, members, we certainly, like the comments of the mayor, we appreciate the opportunity to discuss Senate Bill 961, which is such an important piece of legislation for Hazleton and its residents.

Before I begin into my summary of the testimony, with your indulgence, I would address a couple of issues that I heard in prior testimony. Maybe I can streamline our process today by just responding to a couple of issues this were left open as we go along.

I know, Representative Levdansky, you had requested information about what the intended purpose of the limitation of the remedies back in the '80s were. What was the intention of the municipalities?

This administration obviously was not present and so, on behalf of the City of Hazleton, we are not going to be able to comment on what the city's intentions were, some of the specific remedies that might have been implemented under Act 205 at that time. We can certainly speak to the issues that have occurred since then and as are set forth in our written statements.

There was another question as to whether or not the city is up to its taxing limits, and that is, in fact, the case. It now receives, under the Local Tax Enabling

Act, court approval for the additional 5 percent increase for real estate taxes as it was authorized under the Local Tax Enabling Act.

And, currently, the assessed -- my understanding of assessed valuation of property right now in Luzerne County is at 20 percent of the taxable assessed value. They are currently considering a reassessment. Where those figures will come out, we don't know. But that's where it stands in the county itself.

A question was asked whether or not the City of Hazleton was continuing to use the Act 205 proceeds since 2005 for post-retirement healthcare benefits, and, in fact, that is the case. For calendar years 2006 and 2007, the city continued to use these proceeds to pay for its post-retirement healthcare obligations.

With regard to the liabilities and when they occurred, prior to this administration coming into office two terms ago, as testified by the representative for the Auditor General's office, there were a few contractual labor settlements from a prior administration that did impinge upon the funded status of the plan that's reflected, as Mr. Nickol pointed out, in the current funded status of those plans.

To its credit, this administration took on those benefits, challenged the legal basis for granting them through the courts, and also worked out a resolution with the FOP and the firefighters' union, creating a new benefit structure that has -- on a prospective basis, which complies with the third-class city code.

In fact, this administration received communication from the Auditor General's office in circa 2002, 2003, which commended it for its actions in trying to bring those plans into compliance and bringing costs under control.

And finally, you know, it's nice to actually be in a setting where -- as special labor counsel for municipalities, counsel for the FOP and I don't always see eye to eye on things, but I'm glad to see us here today jointly supporting a piece of important legislation.

I know Mr. Welby has raised a particular issue with regard to the intent of the city regarding the use of these funds. Rest assured, as it has up to this point, it uses and intends to use these proceed for the payment of benefits for employees.

In terms of its ability to discontinue those obligations, we obviously have contractual commitments, enforceable contractual commitments with all of our labor unions to provide those post-retirement healthcare benefits which the city simply cannot walk away from.

So, again, I would try to assuage the concerns in the members of the state FOP regarding the city's intention. Certainly the legislation was passed as a result of an audit finding that identified this misspending as being inappropriately used for post-retirement healthcare benefits.

With those responsive comments, I also, as the mayor mentioned, am encouraged by the support that this legislation has received, not only from PERC, which has commented on its support of this legislation, as well as the Auditor General's office, which sports this legislation.

And I think the mayor had clarified this, but, Representative Scavello, the vote was not 49 to 1; it was 49 to zero in the Senate, so we have a large number on a bipartisan basis of senators that understood and saw the value in this legislation for the City of Hazleton and its taxpayers. And we are hoping the same will be said for the House at the end of the day.

As part of that support, in fact, and as referenced in the written testimony from the Auditor General's office, the department and the city have agreed to hold the pending litigation associated with the audit findings in abeyance.

Representative Ellis mentioned the point that is it a matter of just the city waiting to find out what the end result is of the litigation. The answer is yes. Ultimately, if it's concluded that, after litigation with the AG and whatever appeal level that takes us, the city needs to refund or take some other action relative to the pension plan, it certainly would do so.

But both parties, the Auditor General's office and the city, have agreed to hold this matter in abeyance for the time being to assist this committee and the House in its analysis regarding the import of this legislation and whether or not it, in fact, is a piece of legislation that is deserving of passage.

Unfortunately, it is also our impression that if Senate Bill 961 doesn't pass during this session -- and this is speculation on our part at this point, but even in discussions earlier today with representatives of the Auditor General, it's our understanding that if it does not pass this session, the auditor general will be pushing this back into the litigation mode, at which point we will take the matter out of abeyance and both sides will expend additional money and resources to determine whether or not the actions taken by the city up to this point were appropriate.

Both parties are requesting that this

legislative fix accommodate the audit finding that was issued on behalf of the City of Hazleton.

So, again, we jointly approach this committee to express our universal support for Senate Bill 961. As set forth in the city's written statements that were provided earlier this afternoon, it accomplishes two goals.

First, it will enable the city to continue to use critical funds to its best effect in a narrowly defined set of circumstances by continuing to pay its post-retirement healthcare obligations, which I mentioned, which are contractually committed to under our bargaining agreements with the union.

And, two, it will maintain the protections under Act 205 to ensure that the city's pension plans continued to be funded appropriately and on an annual basis.

As both representatives from the Auditor General's office and from the Public Employer Retirement Commission testified, this is not an amendment to Act 205. The city has an ongoing obligation to meet its annual obligation to fund -- adequately fund all of the pension plan pursuant to that act. And this piece of legislation has no effect on that. It is simply a tax shift of resources to enable the city to use it to its best effect.

As a result of all the foregoing, we're very hopeful that Senate bill receives this committee's full consideration and support.

And so with that, we will be happy to answer any questions.

CHAIRMAN LEVDANSKY: Representative Scavello.

REPRESENTATIVE SCAVELLO: Thank you, Mr. Chairman.

And thank you, gentlemen. You heard in the earlier testimony the solicitor for the FOP recommend that we put a specific amendment in there that it be used for the purpose of pretty much the purposes that you're using it for now. I don't think you'd have any problem with that, if we amended the legislation to include that, but if you read in the legislation, it doesn't have it specifically in here.

MR. MILLER: My comment to that would be I certainly would defer also to the comments from the Auditor General and PERC relative to their interest in any legislation.

I think one of the problems associated with this is, as I said, the timing of this issue is such that if this legislation, which has passed the Senate, is delayed in any way or requires reconsideration, our understanding is, at least at this point, based on the discussions with the Auditor General's office, that they are looking at scheduling this back into a litigation posture sometime this fall.

The theory being if the legislation passes the House as it did the Senate, it renders the entire issue moot, saves the cost and expense both for the Auditor General and the city and any subsequent appeals that may occur.

So my response is that it does have a practical impact in the sense that it's taken so long to get to this point. The indications we have received from the department -- and again, to their credit, up to this point, they have continued to coordinate with the city over the past couple of years while this legislative process has taken place, continued to entitle the city to receive its univalue of state aid, but I believe at this juncture -- and I certainly defer to them to speak on this matter -- I believe at this juncture, they are intent on pulling this back into a litigation posture this fall, so if the legislation doesn't pass now and is required to go back to the Senate, that's where the parties will be.

REPRESENTATIVE SCAVELLO: But normally, if there are questions, and assuming this is what you're going to hear is questions from some of the other members, I personally think that if we can get this done, and if it gets to the Senate, I think there's enough time to clarify that and to make every -- and if we are going to write a bill, let's write it right and make all the parties happy.

I would think that you would need that amendment in there.

MR. MILLER: Again, and not to put

anybody on the spot, but I would defer to the representatives from the Auditor General to see if they would accommodate that kind of process with the city one more time. I know there's representatives from their legal department here.

CHAIRMAN LEVDANSKY: Mr. Miller, I just want to keep this focused. I mean, the Auditor General's office doesn't write legislation. That's our job. And, frankly, you know, they can have their input, but let's not lose sight of the fact that it's the members of the legislature and this committee that is going to make a determination on the substance of this legislation.

REPRESENTATIVE SCAVELLO: Have the legislators and the representatives in your area supported the legislation? I would think that's important. And I see one of the legislators here. I see Representative Eachus here.

Do you have the support of the local legislators?

MAYOR BARLETTA: I can defer to Representative Eachus. I believe he does support the city's efforts as well as Senator Musto on the Senate side.

REPRESENTATIVE SCAVELLO: I think that's important. Thank you very much.

CHAIRMAN LEVDANSKY: Representative Kortz.

REPRESENTATIVE KORTZ: Thank you, Mr. Chairman.

Thank you, gentlemen, for your testimony.

Looking over the numbers that you have provided in your testimony, you used on -- it's page four, $556,000 of the 1.7 million in the year 2003 from the Act 205 revenues. So in that year, if I understand it correctly, your healthcare costs accelerated 33 percent. That's roughly one-third of the money. You saw that much of a jump in your healthcare care in post-retirement other funds?

MR. MILLER: The numbers that are -- and I assume you're referring to question number three?

REPRESENTATIVE KORTZ: Correct.

MR. MILLER: Those are the actual

numbers. Unfortunately, Representative Kortz, the city administrator, who under the optional plan type of municipality that Hazleton is, really, in effect, runs the administration of the city, was not able to be here to testify. He has, obviously, a better handle on all the prior information.

Prior to his departure from the city, he assisted in preparation of documentation. I can't be sure of the exact numbers of post-retirement -- and, again, we're talking about post-retirement healthcare as opposed to active employee retirement healthcare. But that doesn't sound to be an outlandish increase, seeing the types of figures we've seen for post-retirement healthcare increase for municipalities.

REPRESENTATIVE KORTZ: It just stands out. One-third of money as put in the post-retirement.

MR. MILLER: Sure.

REPRESENTATIVE KORTZ: And that continued. It looks like you have spent 5- to 600,000 a year of those three years.

MR. MILLER: Correct.

REPRESENTATIVE KORTZ: Adding up to that number.

Okay. Thank you very much.

CHAIRMAN LEVDANSKY: Chairman Nickol.

REPRESENTATIVE NICKOL: Thank you. I appreciate your addressing the fund ratio, and I had a couple further questions so I better understand when I see the falling fund ratio.

Generally, when you see a falling fund ratio, it's because of benefit enhancement, a reduction in earnings, diminished earnings or reduction in contributions.

What I'm seeing here is for the falling fund ratio, I gather from what you said -- I just wanted to make sure -- that was due to some benefit enhancement such as the ones granted, and I gather because of the impairment contract issue, you couldn't just quickly slide out of them. You could turn things around long term, but short term, they -- I mean, was -- during that period of time, I assume you met your MMO.

MR. MILLER: Correct.

REPRESENTATIVE NICKOL: And with earnings, I mean, it was one of the best bull markets, 2003 to 2007, so the earnings of the pension funds should have looked good, so I can only presume that it was due to an increase in liabilities, probably related to benefit enhancements of some way, shape, or form.

MR. MILLER: Again, I can't speak to the investment return for this particular plan. That would be reflected in a copy of the actuarial report for the municipality, which we can obviously present to this panel, this committee, at a later date.

I would say that certainly there were, because of our firm's actual involvement, after those benefits were granted and the litigate side, to try to bring the plan back into compliance, back at the -- I'm going to say it was around 2001, 2002, that there were increases in benefit costs during that period.

Since this city administration, current administration, has come in, there have not been increases in pension benefits through that -- through the collective bargaining or arbitration process as far as I know. So I would suggest to you it is a combination of both of those things, potential bad market returns, whether or not they met the S and P or some other indicator, I don't know the answer to that, but also certainly would be some increase in the present value of future benefits due to the benefits that were granted several, several years ago.

REPRESENTATIVE NICKOL: I read several reports that PERC has issued with regard to early-retirement incentives. None of these reports were focused on early retirement census state levels. There were all sold as saving money, and the report showed that, in the end, they actually were extremely costly items once granted.

It may reduce salary costs, but what occurs when you have an early-retirement incentive, this often shifts it to retirement -- increase in retirement costs and OPEB costs, because of healthcare, if you have retiree coverage.

And so in the final analysis, you

usually end up losing money. They prove to be fairly costly. Have you assessed what impact -- you seem to have started using the money for OPEB benefits for healthcare at the very same time that you had the early-retirement incentive.

MR. MILLER: What early-retirement incentive?

REPRESENTATIVE NICKOL: The Auditor General talked about early-retirement incentive in 2003, along with the money being used from the special tax for the buy-back of unused vacation and sick leave, which I assume was for people who were taking early retirement, and also that's when you started paying money toward retiree healthcare coverage at the very instant, the very same year, it seems, that the early-retirement incentive was in place.

MR. MILLER: Okay. I would tell you that the post-retirement healthcare benefits predate the current administration and those obligations. I'm not aware of a post -- any kind of retirement incentive that the city offered or granted to its fire or police employees.

What may be referred to, if you're looking at the Auditor General's findings, its findings, there were -- again, and this is going to take a second, but when those original benefits were granted back in the late '90s, before this administration came into office, there were a series of benefits that were well beyond the parameters of the third-class city code, which, as I said, were rectified on a prospective basis by this administration.

One of those benefits was the ability to increase the percentage of the retirement benefit which from which the third-class city code requires 50 percent of final salary up to 75 percent, depending on the number of years of service. An officer retiring after 20 got 50, 21 got 55, so on so forth. After 25 years of service, they got 75 percent benefit.

There was one individual, one or maybe two employees, as I recall, that, because of the contract impairment issue, were entitled to that benefit, 75 percent. They come to the municipality and requested a retirement incentive, leaving two years before their 20th year of service necessity to become superannuation eligible. In exchange, they would only receive 50 percent of final average salary.

When you did the actuarial calculation, the two years of early benefits that they received saved the municipality and the pension plan far more than if those officers had worked to 21, 22, certainly 25 years of service and been entitled to a 50 percent benefit over their lifetime. They were relatively young officers.

So, as I understand it, the municipality in two scenarios, it wasn't a global retirement benefit; it was two officers that they granted additional time to to save the value associated with the illegal benefits that were granted prior to this administration taking office.

Does all that make sense?

REPRESENTATIVE NICKOL: I appreciate that. Because it was really -- in looking to falling ratio and all, I wasn't sure whether Hazleton was continuing to dig its hole deeper --

MR. MILLER: No, to the contrary.

REPRESENTATIVE NICKOL: -- or whether it's trying to dig its way out, and that helps clarify that point for me.

MR. MILLER: And while the AG, again, has taken issue with that -- that grant of those two officers, I think they would readily admit that from an actuarial perspective, it will substantially save the plan value over time as the communication in 2002 did when this administration modified the pension plan to come into compliance with the third-class city code.

REPRESENTATIVE NICKOL: Thank you. I understand your situation a lot better now. Thank you.

MR. MILLER: You're welcome.

CHAIRMAN LEVDANSKY: Executive Director Ritter.

MR. RITTER: Thank you, Mr. Miller.

Who was the -- were you the solicitor for the city in 2003?

MR. MILLER: No. Actually, I have -- to be clear, I've never been the city solicitor. I am just sort of special labor counsel handling personnel and labor matters.

MR. RITTER: All right. In 2003, when a decision was made to use a portion of Act 205 money for OPEB benefits -- and it appeared from PERC that Act 205 does not specifically speak to OPEB liabilities. Did the city seek a legal opinion in 2003 when they made that decision to divert Act 205 moneys to OPEB benefits?

MR. MILLER: My answer to that question -- I do not know the answer to that question. But beyond that, I would say that right now, you do have -- obviously there's litigation between the city. At this point it's amicable between the Auditor General's office and the City of Hazleton regarding this expenditure of money, so I'm going to be a little sensitive to responding to questions that deal with the issue of the appeal of the audit finding between the City of Hazleton and the Auditor General's office.

But to answer that particular question, I was -- I have nothing -- I've never been the city solicitor and I don't know the answer to that question.

I will say this: It is my understanding that the city requested an opinion from the Auditor General's office regarding that issue at the time, at which point the field auditor for the AG confirmed the city's ability to use these assets for purposes of post-retirement healthcare payments, from a field auditor.

They subsequently, I believe, requested a more formal opinion, and I don't know the dates of that, from the Auditor General's office, which, as the case law provides, their standard response was provided, which is, "We do not give preaudit advice."

So, to clarify, it's my understanding that they received advice from a local field auditor regarding the distribution of the fund in a way that they did, but they did not receive that same opinion or any opinion from the department headquarters.

MR. RITTER: All right. Thank you.

CHAIRMAN LEVDANSKY: And was that -- was that a verbal communication between the field auditor?

MR. MILLER: Representative Levdansky, I believe it was.

CHAIRMAN LEVDANSKY: Representative Kessler.

REPRESENTATIVE KESSLER: Prior to the administration that exists now, the 75 percent pension, was that offered to all three categories of employment, do you know?

MR. MILLER: You mean nonuniformed, police, and fire?

REPRESENTATIVE KESSLER: Yes.

MR. MILLER: I believe it was offered to the police and fire.

REPRESENTATIVE KESSLER: And do you know how many people actually got the 75 percent? Is there a number or amount of employees that you know that retired?

MR. MILLER: I do not know -- I do not know, and to the extent it's relevant to this committee for purposes of this legislation, we will get whatever information you deem as relevant, including statistics and figures on those kinds of requests.

I do know that employees, through the

negotiation process -- once the city filed litigation challenging the illegality of the benefits that were granted by the prior administration, several categories of employees were developed -- Class A, Class B, Class C -- which related to the amount of service that they had up to that point up to that point.

I think one of the classes, the Class A individuals, would still be eligible for the up-to-75 percent retirement benefit that was granted in prior rounds of collective bargaining between the city and the FOP.

REPRESENTATIVE KESSLER: Thank you.

MR. MILLER: Sure.

CHAIRMAN LEVDANSKY: Director Kassoway.

MR. KASSOWAY: Under your response to the questions that the committee had submitted, under question one, we asked the rate of the initial special authorization under 205. You indicated a .1 percent in '89. It increased to .5 percent in 1993. And it was subsequently reduced to .4 percent in 1999.

I take note that the legislation requests a rate of .5 percent, which is, you know, 20 percent or 25 percent higher than the rate that's actually in effect now. But being a staffer, I sort of look at numbers. Only $523,000 out of the $1.7 million that was raised in 2007 went to the questionable expenditure. That's about 30 percent of the tax raised. Thirty percent of 1.4 percent would be about .4 percent.

So, really, why do you need a rate of .5 percent to replace .4 percent when only 30 percent of the .4 percent is being used for the questionable items?

MR. MILLER: In response to that question, I would tell you that the city is simply looking for the tax shift that was mentioned by a number of representatives on your committee, which would not even equate to the current -- obviously to the current .4 tax that it takes under 205.

We did not have a final hand in the drafting of the legislation. That was done by, obviously, the Senate and representatives from the Senate, their legislative bureau.

So, my response to you would be, I would not say that there is a need for the .5 that is in the legislation. Certainly, the City of Hazleton, the legislation requires it to shift any amount that it's increasing on the local earned income tax side from the Act 205 tax, that would equate to something less than .4.

MR. KASSOWAY: Going a step further, I think the Auditor General stated earlier that you have approximately, what, $1.5 million that you have to return to them or recharacterize?

MR. MILLER: That's what the audit finding provides for; that's correct.

MR. KASSOWAY: So you could probably raise that in one year's time with the new rate and then reduce the new rate to a lower rate to pay for the healthcare in the future, and then leave some authorization under 205. To me, that seems fairer to the other taxing jurisdictions out there that can't use Act 511 taxes, that can't use -- who don't have the ability to raise additional taxes under Act 205 to help pay for healthcare benefits.

This is giving you the right to use

tax authorization that other taxing jurisdictions don't have to pay for healthcare benefits. What I'm trying to do is suggest that may be the lesser of this special authorization under Act 511, and to retain some authorization under 205 for the purposes stated for 205, and that might be fairer to the others.

You could go that route, or you could go the route that was suggested earlier, just authorizing everybody to have additional authorization to pay for healthcare benefits, but that might be more difficult for the total legislature to buy. But, you know, I'm suggesting somewhere in between.

I just -- it seems difficult why you have to have .5 to replace .4. I can see to pay back some. As I said before, that can be paid back with one year with the amount that you raised.

MR. MILLER: Two things: One, the legislation would result in the city not having to pay anything back. It would, in effect, have authorized what expenditures were made in 2003, 2004, 2005. So there would be no obligation, which might exacerbate the point that was made, but, keep in mind, the way the legislation is drafted, it's a tax shift.

Any increase in the amount that Hazleton would impose under the Local Tax Enabling Act would require a commensurate decrease in its 205 taxing abilities. So -- I understand practically speaking -- and, again, the city wasn't involved in the determination of the percentages that were put into the final bill, but obviously the bill does require to account for the decrease in local 205 tax to offset any increase it would have under the Local Taxes Enabling Act.

MR. KASSOWAY: Does the city have numbers as to how much money is raised from the nonresidents from the tax authorization under 205?

MR. MILLER: I don't know the answer to that question. If it wasn't specifically requested as part of your request for information, not today. Certainly, as I mentioned --

MR. KASSOWAY: Would you get that for

us?

MR. MILLER: We will provide you with any information that would be of public record regarding the tax receipts and our revenues for the city.

MR. KASSOWAY: Thank you.

MR. MILLER: You're welcome.

CHAIRMAN LEVDANSKY: Mayor, I'd just like to put this in perspective. Your whole municipal budget, you know, last year was how much?

MAYOR BARLETTA: We are about $9 million is our budget, and it's about -- a little over $9 million of the general fund. The general fund budget is $9 million.

CHAIRMAN LEVDANSKY: Is $9 million. And you principally -- your revenue source, does that continue to be your city's property tax?

MAYOR BARLETTA: And earned income tax, our two main sources of revenue, both which have fallen.

CHAIRMAN LEVDANSKY: And this special -- this additional tax that's been collected under Act 205, this four-tenths-of-one-percent of the wage tax, you mentioned that it generates $1.7 million. But you only use a little over 500,000 of that to pay for the post-retirement healthcare benefits and I presume a portion of the early retirement enhancement that was offered to get some people to retire, buying out, I think, some of their leave time or what-have-you.

MR. MILLER: I don't know the actual numbers on that, Representative Levdansky, but as Jim McAneny said, it's a very, very small amount compared to the post-retirement healthcare obligation.

CHAIRMAN LEVDANSKY: Okay. What -- so then, if you collect 1.7 million under this four-tenths-of-one-percent wage tax, and you only spend 500,000 of it to pay for the post-retirement healthcare benefits of people in your pension system, where does the other $1.2 million dollars go to?

MR. MILLER: Into the pension plans.

CHAIRMAN LEVDANSKY: Into the pension plan.

Are there any -- are there any salaries or any positions that are funded out of this special four-tenths-of-one-percent wage tax?

MR. MILLER: Could you repeat the question?

CHAIRMAN LEVDANSKY: Are there any -- of the revenue that's collected under the four-tenths-of-one-percent wage tax that you collect pursuant to Act 205 --

MR. MILLER: Yes.

CHAIRMAN LEVDANSKY: -- you're saying that you put roughly 1.2 million of that into the retirement system.

MR. MILLER: Yes.

CHAIRMAN LEVDANSKY: And you use the other 500 -- I'm saying of the 523,000, what all is that used to pay for?

MR. MILLER: Again, not having the luxury of the administrator here, my understanding is those numbers are accurate. The 500,000 was used, prior to being deposited into the pension plan, to pay annual post-retirement healthcare obligations. There may have been a modicum of buy-backs, contractually obligated buy-backs for employees under the collective bargaining agreement. Again, it would be a large part as post-retirement healthcare obligations.

It is also my understanding that the remainder of that money was used and deposited into the pension plans, and I think that's reflected in the Auditor General reports.

CHAIRMAN LEVDANSKY: Are there any uses of these funds, outside of -- these special funds, this special wage tax, is there anything outside of the contribution to the pension system and post-retirement healthcare benefits? Is there any -- is there one dollar or one cent of this special tax authorization used for anything other than contributions to the pension system or contributions to the post-retirement healthcare plan?

MR. MILLER: Again, and if there's something in particular you're referencing, to be repetitive, our understanding is the $500,000 is used -- is taken from the Act 205 tax prior to being deposited into the pension fund to pay for those post-retirement healthcare obligations. The remainder of that money was deposited into the pension plans for those purposes.

CHAIRMAN LEVDANSKY: Now, you mentioned in your testimony in response to our questions that this 523,000 that's used was to pay for the post-retirement healthcare benefits. Is that for 2007? And how does that compare to other years? I mean, given that healthcare costs have varied, have escalated pretty dramatically in the last year or two.

MR. MILLER: My response to that would be, I believe in the audit finding that they prove to be educational in the sense or instructive in that they actually identified the amounts of money that were used for those other benefits.

So, again, off the top of my head, I don't know, but I would tell you that they range between 400,000 and $500,000 between the years 2003 and 2007, 2003 being the first year that money was used in that manner that was the subject of an audit finding, and 2007 obviously being the last year.

CHAIRMAN LEVDANSKY: Okay. I mean -- just another purpose, so you use roughly 1.2 million of the 1.7 to contribute -- to fund your pension system. But the fund ratio of your pension plan has gone down in the last few years. What would be wrong with just using all the money from the allowed sources and from the special source authorized under Act 205? Why not use all of that to fund your pension obligation and to get the fund ratio improved?

MR. MILLER: Again, and I want to be careful not to address issues that are currently pending with the Auditor General's office, but from the city's perspective and its response, it has identified those expenditures for post-retirement healthcare benefits as proper under the Act 205 analysis.

Point number two --

CHAIRMAN LEVDANSKY: I'm sorry. Who said that's been proper under Act 205? The Auditor General?

MR. MILLER: No. In response -- the city's response, that's the reason we're in litigation on that. The city's response to the Auditor General findings is that those claims are appropriate under Act 205. That's the purple of the legislation is to address the litigation that is pending between the department and the city.

But let's assume, for the sake of argument, that that's not the issue. If it doesn't use that money for post-retirement healthcare obligation, it's at its tax limits for all revenue sources combined. If there was other resources available to pay those contractual obligations, it would do so.

CHAIRMAN LEVDANSKY: I understand. When was the last time Luzerne County did a reassessment of the property?

MR. MILLER: I don't know the answer to the question on when the county --

CHAIRMAN LEVDANSKY: Mayor, do you have any idea?

MAYOR BARLETTA: It was 40 years ago. They're going through reassessment right now.

CHAIRMAN LEVDANSKY: Forty years. You haven't been reassessed for 40 years. Is it any wonder that most municipalities are at their statutory cap?

MR. MILLER: That's certainly another

discussion for another day. We would agree that there's --

CHAIRMAN LEVDANSKY: Not only another discussion, but it could be a solution to your problem.

MAYOR BARLETTA: Unfortunately --

CHAIRMAN LEVDANSKY: The reality is you are at your caps because you haven't reassessed for 40 years. If you reassess and set values went up, millage would come down, because of the -- you are required to be revenue neutral with the exception of municipalities can receive up to a 5 percent increase in revenue.

So, basically, you're going to be revenue neutral. Millage is going to go down.

MAYOR BARLETTA: There's some objection to the reassessment right now in Luzerne County, so it hasn't moved forward, and actually might be -- one possibility it may be scrapped, and so the -- that solution may be down the road years.

CHAIRMAN LEVDANSKY: And take it from somebody that comes from a town that struggled through reassessments, but the reality is, we've done that in Allegheny County in order to try to get our assessments more accurate.

And the fact that other counties do it once every 40 years doesn't obviate the need to do this, if only to enable municipalities and school districts to keep their tax millages below the statutory caps.

MAYOR BARLETTA: And city -- and all cities would have that ability to decrease their taxes at that point when and if it ever becomes a reality, but the matter that the City of Hazleton is faced with is that we are -- the citizens are taxed to the maximum allowed by law. And without using those moneys, again, the city would be forced into Act 47, which would not help the commonwealth, would not help the citizens of Hazleton, would not help the employees. Nobody wins if that's the solution to this problem.

We're here today with support for legislation from the Auditor General, from the employees, and, again, from the Senate and PERC to a solution to a problem that Hazleton's facing.

MR. MILLER: And we wouldn't -- I mean, to be clear, I don't think the City of Hazleton would turn away from any possible solution to its issues. In fact, it has turned over every stone, as referenced in the communication that we received from the Auditor General's office less than five years ago. It has done everything it can to maintain its fiscal integrity and to get back onto a course -- a prudent financial course for the taxpayers and residents.

It wouldn't turn its back on any kind of solution. The one that we are presented with today is Senate Bill 961, which we do think addresses the issue appropriately.

CHAIRMAN LEVDANSKY: Mr. Miller, the other concern that I have, I mean, is just with the fact that in Act 205, the authorized -- the imposition of an additional wage tax for a very specific purpose. And I appreciate the dilemma which confronts you, but the fact is that in this particular case, the city used that extra taxing authority to levy a tax to pay for post-retirement healthcare benefits, which are not -- were not and are not an authorized expenditure under Act 205.

Other municipalities have pressing financial problems just as Hazleton does. And we've learned that Altoona, for example, you know, was also in a bind. And they had to make adjustments to come into compliance with the law, with the statute. And I just -- you know, I just have a real uncomfortableness and concern about changing the law for one particular municipality and to do so retroactively.

And I'm not a -- I'm not a statutory construction attorney.

MAYOR BARLETTA: If I may --

CHAIRMAN LEVDANSKY: I think there are some real concerns relative to that.

Let me finish up, Mayor, then I'll recognize you.

So my greater concern is that we're just trying to solve one problem for one municipality, when the reality is, there are other municipalities and other pension systems that would probably like to afford themselves of this option too, but they read the law and recognized that they couldn't fund anything outside the pension benefits with these funds. And they followed the law. So why should we penalize people for following the law?

MR. MILLER: You asked the ultimate question, Representative Levdansky. It's not clear, in fact, that's what the parties are attempting to avoid. With the support of the AG, we are attempting to avert whether or not that determination even has to be made.

You know, as Mr. McAneny mentioned, a recent Commonwealth Court decision less than -- just a few months ago cited the definition of provisions of Act 205, and again, I would tend to agree that there are certain factual distinctions between that case and this.

But a member of the Commonwealth Court defined a "retirement system" to include a post-retirement healthcare fund under Act 205. To say that the municipality intentionally skirted the law, and that was clear, I just disagree with.

And we're not here, again, to debate

the merits of that case. You certainly obviously have a position regarding whether or not they were complying with the law or not. That's what ultimately we are going to decide when we get to --

CHAIRMAN LEVDANSKY: And this has been going on since 2003 or before?

MR. MILLER: Correct.

CHAIRMAN LEVDANSKY: And when was that court decision made that raised the ambiguity?

MR. MILLER: It didn't raise an ambiguity; it confirmed --

CHAIRMAN LEVDANSKY: Your interpretation of it.

MR. MILLER: Correct.

CHAIRMAN LEVDANSKY: And when did that court decision come down?

MR. MILLER: This year.

CHAIRMAN LEVDANSKY: This year?

MR. MILLER: Correct.

CHAIRMAN LEVDANSKY: So that Hazleton's been collecting this since 2003. And I respect that. So don't use a court decision that came down this year as a justification for collecting this. You have been collecting this since 2003.

MR. MILLER: The decision was -- if the issue came to the court in 2003, it would have been the same decision. The timing of the case isn't relative to the city's position in the litigation.

CHAIRMAN LEVDANSKY: Do you have an opinion from the solicitor justifying that interpretation?

MR. MILLER: Again, as I responded to Representative Ritter, I was not -- I've not been the solicitor, I'm not the solicitor, was I then or am I now. So I do not have an opinion on that.

And I would tell you that if there were any comments from the solicitor regarding whether or not that was authorized, it would be privileged.

I will say, once again, when the city requested some type of advice from the Auditor General's office, again, at the local level, at the field auditor level, we received it. And that notification was it would be an appropriate expenditure.

CHAIRMAN LEVDANSKY: I never hang my hat or determine anything based on a recommendation or an interpretation from any field person, not just in the Auditor General's office but anywhere. Something this grave and this significant, you need to have it -- the understanding, the legal interpretation, in writing from somebody in authority within that agency.

Just want to recognize the mayor.

MAYOR BARLETTA: Thank you.

If I could just go back to your point there. If the commonwealth could pass a law that doesn't harm anyone but helps even one city, why would we not?

CHAIRMAN LEVDANSKY: Because there are other municipalities similarly situated that have -- have made the tough decisions to fund post-retirement benefits with other sources, come out of general funds. They probably made tough decisions to not spend in other areas in order to fund those post-retirement benefits.

So that's -- Mayor, that's what we're looking up against. We are looking up against on all other municipalities, third-class cities, struggling just like yours, that have made tough decisions to fund post-retirement benefit through general fund obligations, which is the legal and correct way to do it.

Any other questions?

Mayor, I want to thank you and your legal team for being here with us. This is obviously a really -- you know, a complex issue, but we appreciate your testimony here today as we work to try to achieve some reconciliation.

MR. MILLER: Thank you, Mr. Chairman.

MAYOR BARLETTA: Thank you.

CHAIRMAN LEVDANSKY: Mr. McAneny, are you still here?

MR. MCANENY: Yes, I am.

CHAIRMAN LEVDANSKY: Members have a few other questions.

Thank you, Mayor.

MAYOR BARLETTA: Thank you.

MR. KASSOWAY: A very simple question. We've heard how you had to aggregate your funds. Why, then, do we have these separate showing the police, fire, and nonuniformed separately listed?

MR. MCANENY: The aggregation of funds under Act 205 was solely for the purposes of investment and administration. You still maintained the separate accounts of each fund. So there's truly separate funds as far as their liabilities are concerned, their assets are concerned, but in order to get the economies of scale, the act requires that they combine them just for purposes of investment and administration. So it is sort of limited aggregation.

MR. KASSOWAY: And that's clearly defined in the legislation?

MR. MCANENY: Yes, it is.

MR. KASSOWAY: Thank you.

MR. MCANENY: The only place in Pennsylvania that has a true aggregated fund is Philadelphia, and that's because that's the way their home rule charter set it up.

MR. KASSOWAY: Thank you.

CHAIRMAN LEVDANSKY: Director Ritter.

MR. RITTER: Thank you.

Mr. McAneny, couple last questions.

I think earlier in your testimony you asked or you suggested OPEB liabilities are not specifically statutorily discussed anywhere in Act 205. Is that accurate?

MR. MCANENY: That is accurate.

MR. RITTER: In light of GASB 45, has -- I guess, once municipalities start reporting their GASB 45 liabilities, is that going to be accounted as a liability of the pension system or a separate liability?

MR. MCANENY: No. GASB 45 does not suggest that it should be a liability of the pension plan nor does Act 205. It will be reported as a liability of the municipality under the municipality's financial statements just like the pension liability is reported as a liability in the municipality, but they're two distinct liabilities. One will be for the pension; one will be for the OPEBs.

MR. RITTER: And prior to 2003, PERC never issued an opinion clarifying Act 205 to that regard? Or -- you know, to help provide guidance to these Act 205 municipalities who may have been considering such a -- such a contribution for their OPEB liabilities.

MR. MCANENY: Prior to Hazleton doing this, that was the first that the issue had ever been raised and brought to PERC's attention.

MR. RITTER: Okay.

MR. MCANENY: And that actually got brought to our attention by -- directly by the Auditor General.

MR. RITTER: I got you. Thank you.

MR. MCANENY: There is no way for us to get it.

MR. RITTER: Sure.

MR. MCANENY: If I may, I have one point I just wanted to make sure that the committee understands. Act 205 liabilities are not just pension liabilities; they're the specific annual contribution requirements that the municipality has to make.

So I could go out and assess a 50 percent income tax under Act 205 and put it all in the pension plan, and that doesn't make it legal just because I put it in the pension plan, because it wasn't part of the -- it wasn't the required payment to the pension plan for that year.

You can't just go out and collect any amount of money you want to and put it in the pension and say that's automatically allowed. That's not what that tax is for.

MR. KASSOWAY: I don't know if the gentleman for the Auditor General's office would like to join you at the table, but I have one question for the two of you.

Since I'm told that the two of you had dealings with drafting this legislation, why was it decided to authorize -- why was it decided to not only authorize .5, but to establish the rate at .5 percent in order to eliminate a .4 percent tax, which is 25 percent more than needed?

MR. MCANENY: First of all, the act does not establish the .5. It is up to .5. It is up to five-tenths. That is the maximum.

If you look at lines 27 and 28 on the second page of the bill, it's rates of taxation of earned income up to an additional five-tenths percent beyond the maximum rates. So it's not an automatic five-tenths; it's up to five-tenths.

Why was it put at five-tenths? The original bill was not a Hazleton-only bill. It didn't have this senseless language that restricted it just to Hazleton. This would have been available to anyone, any municipality, that was at their maximum tax rates and had an Act 205 tax. So it wasn't just Hazleton when the thing was first drafted.

MR. KASSOWAY: Where was it amended?

MR. MCANENY: Where was it amended?

MR. KASSOWAY: Where was it amended, in committee or on the floor?

MR. MCANENY: I have no idea. They didn't -- they didn't consult me.

CHAIRMAN LEVDANSKY: Gentlemen, thank you.

Hold on. Representative Vulakovich.

REPRESENTATIVE VULAKOVICH: Let's say we keep this scenario exactly the same, that we would pass this and they would get the .4. Let's say theoretically they raised 1.742 million. Where in this legislation does it say how they're going to break that down, what they're going to spend that money on?

MR. MCANENY: It doesn't. Other than the fact that it has to be used to offset the Act 205 tax. So you have to stop collecting that one.

This doesn't dictate where the money gets spent. It dictates that it's to be used to replace money that they're already collecting under a different statute.

REPRESENTATIVE VULAKOVICH: So they could or could not take 500 -- using the same stats -- they could or could not take the 523,000, they may not spend it on healthcare, which --

MR. MCANENY: They're going to have to spend a 500,000 on healthcare somewhere from some source.

REPRESENTATIVE VULAKOVICH: Right. So the difference between 1.7 million and the 523, there's that money there.

MR. MCANENY: Right.

REPRESENTATIVE VULAKOVICH: Now, because the reason --

MR. MCANENY: This is why it has --

REPRESENTATIVE VULAKOVICH: It seems to me where it should go.

MR. MCANENY: It doesn't have to go to the pension.

REPRESENTATIVE VULAKOVICH: I realize that.

MR. MCANENY: And so you understand, a lot of the money that Hazleton did put into their pension was not required to be paid by Act 205. It was funded over and above the minimum municipal obligation. So they did put extra money into the pension plan that they otherwise were not required to put in in any given year.

REPRESENTATIVE VULAKOVICH: So they complied with their MMO.

MR. MCANENY: And then some.

REPRESENTATIVE VULAKOVICH: And then they put the difference of this money between the 523 and the 1.7, the difference they put in their pension plan.

MR. MCANENY: Part of it was the MMO and part of it was over the MMO, right.

REPRESENTATIVE VULAKOVICH: Okay.

MR. MCANENY: So they used the money just to put into the pension plan. It covered the MMO, and it did some more. And I'm not --

the original draft of the legislation was intended to provide a method for municipalities who were capped at the maximum tax rates already and who were assessing an Act 205 tax a way to get away from the Act 205 tax and utilize a tax which had court approval, and that process, as opposed to the "nobody supervises it" provisions under Act 205, because nobody looks at that. That not voter approved. That's not court approved.

And the attempts to get rid of -- I guess Representative Nickol introduced the bill for our commission to repeal Chapter 6 of Act 205. It's probably in this committee. But it just hasn't moved. And it's been a couple of sessions now and it never moves. So I don't know if it ever will.

So we can't get rid of the Act 205 tax, so we're trying to find ways to move people away from it and into a more transparent form of tax. Court approval is also better than no approval. A cap of five-tenths-of-a-percent is better than no cap at all, which is what we have right now. We have uncapped, unsupervised tax.

REPRESENTATIVE VULAKOVICH: Okay. Thank you.

CHAIRMAN LEVDANSKY: Additional questions from Director Kassoway.

MR. KASSOWAY: Actually, Mr. Bergen, first, we'd like to have you comment on the field auditor's opinion that we issued back when.

And, secondly, it was stated that they didn't -- that Hazleton did not have to repay any of the moneys or redirect them with the additional money they're getting here. I was under the impression they did. I'd just like to have that clarified on the record.

Thank you.

MR. BERGEN: Okay. First of all, as to the field auditor's comment, you know, we are not aware of any advice that a field auditor gave to anyone in the city. You know, certainly we don't have anything documenting that.

As far as the second part of your question, I believe what I was referencing is if the bill passed, then the reimbursement would be moot in terms of the prior audit report. Is that what you were referring to?

MR. KASSOWAY: Somewhere along the lines I thought, in discussion or reading one of the reports, it was indicated to me that part of the justification for the tax rate was that whatever money had been directed to the health benefits would have to be redirected to the basic requirements under the act, and that then the health benefits would be picked up with the new authorization.

I just wanted to clear my mind whether or not there actually needs to be any movement of moneys in the pension fund or not.

MR. BERGEN: The audit report recommended that the tax fund or the pension plan be reimbursed for the money that was -- that was spent from the special tax. So beyond that, I just want to make sure I'm understanding your question.

MR. KASSOWAY: That's the question that was in my mind, whether that's an actual transfer of money, or if, with the language in the act which says that the prior expenditure of 205 shall -- the money raised by 205 shall be considered being raised with this new levy, if that would somehow affect that result, or do they have to take the first $1.5 million that they raise under this new levy and pay back into the -- I guess that there are different -- as it's stated, there's different purposes. I mean, the health is one fund or one trust or whatever, and the benefits funds would be a separate one.

Do they actually have to transfer money into the benefits? You know, into the retired 205 --

MR. BERGEN: Under Senate Bill 961?

MR. KASSOWAY: Right.

MR. BERGEN: No. It's my impression, no.

MR. KASSOWAY: Okay.

CHAIRMAN LEVDANSKY: Thank you, Mr. McAneny, Mr. Bergen, and everyone else that testified.

Mayor, thanks for coming down from Hazleton and welcome all of your insights. Thank you.

3:56 p.m.

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REPORTER'S CERTIFICATE

I HEREBY CERTIFY that I was present upon the hearing of the above-entitled matter and there reported stenographically the proceedings had and the testimony produced; and I further certify that the foregoing is a true and correct transcript of my said stenographic notes.

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BRENDA J. PARDUN, RPR
Court Reporter
Notary Public