COUNCIL OF THE CITY OF PHILADELPHIA

COMMITTEE ON FISCAL STABILITY AND

INTERGOVERNMENTAL COOPERATION

Room 400, City Hall
1400 John F. Kennedy Boulevard
Philadelphia, Pennsylvania 19107
Tuesday, February 25, 2020
10:15 a.m.

PRESENT:

COUNCILMAN ALLAN DOMB, CHAIR
COUNCILMAN BRIAN O'NEILL, VICE-CHAIR
COUNCILWOMAN KATHERINE GILMORE RICHARDSON
COUNCILMAN DEREK S. GREEN
COUNCILWOMAN CINDY BASS
COUNCILMAN MARK SQUILLA
COUNCILWOMAN HELEN GYM

RESOLUTION: 200039

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COUNCILMAN DOMB: This hearing is called to order. And to my immediate right is Councilmember Kathy Gilmore Richardson. To my immediate left is Councilmember Derek Green. This is the public hearing of the Committee on Fiscal Responsibility Intergovernmental Cooperation.

The purpose of this public hearing is to hear testimony on Resolution 200039 sponsored by Councilmember Gilmore Richardson. The Clerk will now please read the title of the resolution before the Committee today.

THE CLERK: Authorizing the Committee on Fiscal Stability and Intergovernmental Cooperation to conduct hearings to determine the City of Philadelphia's preparedness for the possibility of an economic recession and the strength of the reserve stabilization funds.

COUNCILMAN DOMB: The Chair

would like to recognize Councilmember Kathy Gilmore Richardson for some remarks.

COUNCILWOMAN GILMORE RICHARDSON: Thank you, Mr. Chair. Good morning. I want to thank you, Mr. Chair, and our Vice-chair Councilman O'Neill and Councilman Green and all of our colleagues here this morning. I also want to thank our panel of witnesses who are here to share their experience with us this morning.

This is an important hearing to have, particularly just a few short weeks before the Mayor's budget address to this Council. What I hope we can gain from the testimony today is a sense of where our City stands in regards to preparedness to whether another recession as well as suggestions for how the City can be ready going forward.

Last year at the end of the fiscal year as a result of careful budgeting and responsible spending, the City had a surplus. Based on Quarter 2 projections, we anticipate having another surplus this year, and it's more than earlier projected, but less than we ended with last year.

Many stakeholders will see this surplus as an opportunity to ask for more and to spend more money. As duly-elected representatives of the people of Philadelphia, we are charged with being responsible with our City's finances.

In 2007, the nation entered into an economic recession then called the Great Recession. Bank stops issuing loans, businesses failed and our City's revenue went abruptly downward. We were ill-prepared for the ramifications that come with an economic recession and it is our responsibility now to learn from our past mistakes and to ensure that our City is prepared to weather whatever comes to us, particularly from the standpoint of how we spend and save our City's revenue.

Since 2007, we have taken steps to prepare. The City has four reserve funds which we'll hear more about later. And while it is important to ensure that we allocate funding for the essential functions of running our City, it is our role to ensure that we prepare for the event of an economic downturn.

And on a point of personal privilege, I just want to mention that I was a legislative aide here in City Council here during the last recession and I remember a lot of the tough choices we had to make during that time and looking at the services we provide as a city and how we were going to continue to be responsive to our constituents and I never want to have that feeling ever again.

I remember having to do a bill at the very last minute in June, I believe, for the District around $30 million, during that time for the School District of Philadelphia. And I think now that we have a surplus it's a great opportunity for us to talk about how we prepare for any potential economic recession that may come our way.

So thank you all so very much for being here. Thank you for the opportunity to have this discussion. I'm going to use this as a framework as we go into our budget hearing and I look forward to the outcome of this hearing in sharing that information with all of my colleagues from Philadelphia City Council. Thank you very, very much.

COUNCILMAN DOMB: Thank you, Councilmember Gilmore Richardson. It's a very important topic and we appreciate you bringing this forward. Will the Clerk please call the first panel of witnesses?

THE CLERK: Harvey Rice.

(Witness approached

Witness Table.)

COUNCILMAN DOMB: Please state -- good morning.

MR. RICE: Good morning.

COUNCILMAN DOMB: Please state your full name for the record and proceed with your testimony.

MR. RICE: Harvey Rice, Executive Director of Pennsylvania Intergovernmental Cooperation Authority. Good morning, Chairperson Domb, and members of the Committee. Thank you for allowing me to testify on Resolution No. 200039 today regarding the state of the reserve fund and the City's ability to weather an economic downturn. Although the City is on better fiscal footing than it has been for years or maybe even decades, PICA does not believe it is in the strongest financial position to weather a severe economic downturn.

As you know, PICA annually reviews and approves the City's five-year plan. And in our staff report on the five-year plan, we identify key risks that can impact the City's plan over the next five years. In our staff report on the current five-year plan, we identified economic growth or a potential lack thereof as a key risk that might impede the City's ability to realize the projected revenues.

Fortunately to date, the economy has continued its expansion and therefore City tax revenues are coming in as projected, if not even higher. However, we all know this good fortune will not last forever and City officials have been taking measures to protect our City from any possible future decline in revenues due to an economic slowdown.

PICA has long advocated for a rainy day fund to prepare for an economic slowdown. As such, we were pleased when City Council adopted the budget's stabilization reserve fund or rainy day fund back in 2011. Unfortunately, it took another nine years to initiate the funding of the reserve.

As part of the current '20 to '24 five-year plan, the City made its first ever deposit of $34.2 million with an additional $146.5 million projected to be deposited by the end of the five-year plan for a total of $180 million. However, even this five-year projection would only pay the City's payroll for a matter of weeks should revenue plummet during a significant economic downturn.

Additionally, there's a possibility as we have seen in the past that the BSR contributions may not be funded as originally projected. For instance, in past plans where the City has projected contributions to the BSR, other contingencies have taken precedent which ultimately eliminated contributions to the BSR.

Furthermore, we are concerned that the expiring labor contracts for all eight labor unions upcoming at the end of June 2020 might result in more foregoing BSR contributions in the future plan. Hopefully, we will see this commitment to fund the BSR will continue in the FY 21, 25 five-year plan.

PICA has also advocated for voluntary contributions to the BSR even if the revenue threshold that would trigger deposit is not met. Another factor to be considered when assessing the City's preparedness for an economic downturn is the general fund balance.

In FY 2019 the year-end fund balance was $438.6 million or 9.2 percent of general obligations. This was $140.9 million more than projected -- more than the projected $297.7 million, and signified the second time the City met or exceeded its internal target for a fund balance, which is between 6 and 8 percent of obligations. Despite the recent larger fund balances since 2018, higher projected fund balances in the '20, '24 five-year plan, fund balances remain below the Government Finance Officers Association, the GFOA recommendation of 17 percent of obligations.

As mentioned previously, the City has established an internal target fund balance of 6 to 8 percent of obligations. In the current 2024 plan, the City projects fund balances to range from 4.2 percent of obligations in FY 20 to a low of 2.5 percent in FY 22.

Therefore, if an economic downturn occurred, higher fund balances would help the City lessen the impact on City services in the short term. PICA recognizes the City's effort to ensure larger fund balances in the current plan and hopes the City will continue this direction by increasing fund balances to meet GFOA recommendations.

In recent five-year plans, the City has also established a contingency for federal funding cuts which represents money set aside in the event of potential federal cuts to grant money. PICA advocated for such a contingency planning at the beginning of the current presidential administration. However, although the risk of funding cuts from the federal government has been minimal to date, the City continues to set aside money in this reserve.

Going forward, the City plans to use this reserve as a contingency for a recession or economic downturn. We must keep in mind that this reserve along with the provision for future labor costs are included in the year-end fund balance.

In conclusion, although the City has made significant strides towards short-term fiscal stability, overall that's not sufficient to weather a severe recession or economic downturn. PICA will continue to monitor the City's commitment to higher fund balances and contributions to the

City's BSR to better prepare us for a an economic downturn. Thank you for allowing me to testify and I'm available to answer any questions that you may have.

COUNCILMAN DOMB: Thank you for your testimony, Mr. Rice. I have two questions and then I'm going to turn it over to my colleague Councilmember Derek Green.

In your opinion, is the biggest financial burden on our budget the pension obligation?

MR. RICE: I would say, yes, it is one -- if it's not the biggest, it's one of the top biggest drains on the City's General Fund.

COUNCILMAN DOMB: And currently, does that represent in the neighborhood of 16 to 17 percent of the annual budget?

MR. RICE: Yes.

COUNCILMAN DOMB: And if that was funded, how much would that represent of the annual budget? If it was fully funded, what would be the annual percentage of the annual budget?

MR. RICE: I'm not sure of that. I would have to check that out.

COUNCILMAN DOMB: Okay. And then last but not least, has there --

MR. RICE: We're at $6.1 billion on funded liability. We're 46.8 percent funded of the pension.

COUNCILMAN DOMB: Okay. Have we given any thought, is there any possibility of utilizing assets that the City owns in exchange for not having to pay obligations and pledging those assets as part of that requirement?

MR. RICE: We just started to look into that within just a few weeks, so I really don't have an opinion on that yet. I mean, there's always once an asset is sold and you have that money is then used and gone, so we have to weigh that.

What we also think is, and I think Council has talked about this, pilots with nonprofits and institutions, that maybe something like that can help generate more revenue into the rev --

COUNCILMAN DOMB: But what I'm talking about, I think other states have done this, they pledge assets instead of making payments against the obligation. That frees up the cash. And I guess my point in bringing this up is that could be a contingency plan in case we did have a downturn or we can even look at it now, but that could be one of the contingency plans that we could put in place.

MR. RICE: As many contingency plans we can have in place to ensure that when a recession or an economic downturn hits, that we have more money, revenues and funds are available to weather that storm.

COUNCILMAN DOMB: Okay. Thank you for your testimony. Councilmember Green?

COUNCILMAN GREEN: Thank you,

Mr. Chair. Thank you, Mr. Rice, for being here. Thank you for your work at PICA. Your testimony echoes some of the information that we talked about a few months ago when we had the one day conference with PEW, and I think your testimony information you presented with PICA once again reinforced the need to make sure that PICA stays in existence.

As we all know, the enabling legislation for PICA will expire 2023. We'll be continuing the conversation that I started regarding the future PICA through hearings. We also know the impact of what would occur to the City of Philadelphia if that enabled legislation were to not to stay in existence.

Further, as I stated in the past and I still believe we need to have an independent fiscal office in the City of Philadelphia. Some would call that a local congressional budget office. I see that as a possible role for PICA in the future as we look forward to re-authorizing the PICA legislation, but that's a conversation for another day.

But I wanted to focus a little bit more on your testimony today. And you made reference to a couple of key points. One, the federal contingency that we've been carrying for about $50 million for the past couple of years since this current administration came into office.

One of my questions, considering that our fund balance has been higher than in the past years but still not at the level it should be based on cities of our size or based on GAO recommendations, would you suggest we increase that federal contingency or do you think that's the right size at this point?

MR. RICE: If we're going to use that as a recessionary reserve, I would increase it. I would recommend increasing it.

COUNCILMAN GREEN: Well, not necessarily as a recessionary reserve, although it could be used for that if we do get to a recession. But considering the fund balance has been higher than it has been in the past and you know this has come -- we have a need to put more money into the rainy day fund or the stabilization reserve, but at the same point you don't want to put something in there and then take it out so --

MR. RICE: But if --

COUNCILMAN GREEN: So would you think it would make more sense to put additional dollars or budget additional dollars for that contingency fund?

MR. RICE: Yes, because at the end of the year that is rolled over into your fund balance so that would make the fund balance bigger and it's better budgeting and better planning.

COUNCILMAN GREEN: Okay. And have you had any thoughts on what that additional amount should be?

MR. RICE: I haven't. We haven't looked at that.

COUNCILMAN GREEN: Okay. Maybe and as you continue to look at the five-year plan, that's something that you may want to opine on at some point in the future. Also, in reference to the BSR or the budget stabilization reserve or rainy day fund, do you think the trigger for that should be changed?

You made reference to the fact that it was adopted, but it was about nine years before any deposits actually went into the BSR. Do you think that number or the -- I'm sorry, that trigger should be changed at all?

MR. RICE: I don't know yet. I remember in -- it was the budget for FY 19. If the City would have put $2 million more, it would have triggered a contribution of the BSR. So if they would have lessened the federal reserve by $2 million or raised the revenue projections, so we would have had -- at that year we would have had a contribution of BSR. But I haven't looked at what that level would be a good level.

COUNCILMAN GREEN: You made reference to our City of Labor contracts which are coming up. And although we're not projecting onto recession at this moment, we have been in a very long -- market, one of the longest that we've had in the history of this country and we are going through some significant pressures from the impact of the coronavirus which will probably depress manufacturing and also the import, export market at least probably going to the third quarter or maybe the fourth quarter.

If you look at GDP for the country, it has not been at the robust levels that some who are currently in office would like to see. I think part of that is that we are a very mature country. Workforce is aging. As my father would say, it's seasoned.

And so, when you look at all of those factors, do you have any concern in reference to the ability to address some of the issues in our labor contracts as well as all of the fiscal concerns we have and from a global perspective and back in Philadelphia, even though we're not right at a recession, we could be at a short-term period?

MR. RICE: Could you ask the question again?

COUNCILMAN GREEN: Your concern to reference from the bill they put additional dollars, even the budget stabilization reserve or the federal contingency considering some of the maturations I talked about and at the same point we had the pressures of resolving our labor contracts.

MR. RICE: I remember when I was first appointed Executive Director at PICA, I think the first plan I saw there was no labor reserves, there was no money for labor contracts. And so, working with the City we said this is not acceptable, you need to at least put something in there understanding the dynamics of how much do you put in and then what becomes the starting point for any labor negotiations.

In this plan, I think there's $140 million over the life of the plan for labor cost and we projected a conservative that a $240 million over the life of the plan. That's a 2 percent conservative raise, so that would be like $102 million more than what the City has already put in as reserve. So I would use that as a starting point.

COUNCILMAN GREEN: And one last question, do you have any concerns in reference to the current status of the School District considering that out-years of the five-year plan, the School District will have some significant financial issues from the perspective of having a negative deficit that becomes pretty large in the out-years --

MR. RICE: Right.

COUNCILMAN GREEN: -- and that impact will have on the City of Philadelphia from our ability to deal with both the labor contracts as well as trying to increase our fund balance and also provide more dollars into the rainy day fund as well as maintaining the federal contingency.

MR. RICE: Yes. The School District's situation in the out-years going forward was a risk that we saw when we analyzed the current five-year plan and issued our report on it because it shows deficits in 2022 of $76.4 million rising to $186 million in 2023 and almost $300 million in '24. So with the City's commitment to fund the School District and local control, we saw that as a risk to the plan.

COUNCILMAN GREEN: Okay. Thank you, Mr. Chair.

COUNCILMAN DOMB: Thank you,

Councilmember Green. And I want to recognize some Councilmembers that have joined us, to my immediate right Councilmember Cindy Bass and to my left, Councilmember Mark Squilla and the Vice-chair of the Committee, Councilmember Brian O'Neill. Thank you.

MR. RICE: Thank you.

COUNCILMAN DOMB: Thank you for your testimony. I appreciate it and thank you for all your work at PICA too. Thank you very much.

MR. RICE: Thank you so much.

COUNCILMAN DOMB: Will the Clerk please call the next panel?

THE CLERK: Marisa Waxman.

COUNCILMAN DOMB: Please state your full name for the record and proceed with your testimony. And I want to acknowledge, I believe I see your mom here too.

MS. GOREN WAXMAN: Thank you. Good morning, Chairperson Domb, and members of the Committee on Fiscal

Stability and Intergovernmental Cooperation. My name is Marisa Goren Waxman and I'm the Budget Director for the City of Philadelphia.

Thank you for the opportunity to come before you today to talk about the City's fiscal health. With me is Rob Dubow, the City's Finance Director. I'll cut right to the chase. We are better prepared for the next recession than we were for the last one thanks to intentional actions by the Administration and City Council, but we still have tremendous weaknesses in our fiscal health.

These weaknesses will put at further risk vulnerable Philadelphians who rely upon City services in the next recession when demand for those services can be expected to grow. Given this reality about our current fiscal condition and the needs of Philadelphians, it is essential that we continue to be intentional about improving our fiscal health as a city.

Right now we are in a prolonged period of economic expansion allowing the City to recover from the last recession by investing more in City services while at the same time shoring up our longterm fiscal health by creating reserves for future needs.

The City's economic consultants expect a national and local economic expansion to continue a bit longer with just a 25 percent chance of a recession in 2012, but our chances of making it through the entire FY 21 through 25 five-year plan without a downturn are slimmer.

In a recession, we can expect that revenues will decrease. Our fixed cost already a significant portion of the City budget would stay the same or even grow and demand for City services will grow. With our high poverty rate, weak tax base and large fixed cost, Philadelphia remains vulnerable to a recession.

When evaluating our most

recent general obligation bond issue in November 2019, Moody's noted "some persistent weaknesses like the City's very high poverty and above-average unemployment rate." Two of our biggest fixed costs, debt service and pension payments, account for over 20 percent of our budget. That means if we have to make choices about how to react to a recession, one-fifth of our budget will be untouchable.

Even with those high fixed costs, the City is better positioned with the next recession compared to the last one. We've taken a number of steps to get here. These include stress testing our budget, increasing pay-as-you-go capital spending, increasing our fund balance and setting aside reserves.

In late fall, we analyzed the impact on revenues during the last three recessions to assess the scale of losses we could expect under different conditions given our current level of reserves. If revenues grow half as much after FY 20 as what we currently anticipate through FY 24, Philadelphia would lose $263 million in revenue compared to the adopted five-year plan.

If revenues do not grow at all after FY 20, Philadelphia would lose $1.3 billion compared to the adopted five-year plan. And if revenues declined by 3 percent in FY 21 and FY 22 and then hold steady in FY 24, Philadelphia would lose $1.9 billion compared to the adopted five-year plan.

In all but the mildest recession scenario, the City's fund balance could quickly turn negative with deficits that's over $100 million as early as FY 22 and the City would be forced to make painful budget choices. Our pay as you go funding for capital projects with operating dollars rather than by issuing debt avoids borrowing costs by addressing critical infrastructure needs.

We have increased the fund balance in recent years, meaning even slightly exceeding the Administration's goals of 6 to 8 percent of expenditures. The City ended FY 19 with a fund balance of $439 million, 9 percent of the budget.

While this is a significant improvement, I must point out that it falls far short of what other major cities do and of the Government Finance Officers Association recommendation of 17 percent of fund balance, enough to pay two months of City bills.

Philadelphia has set aside other reserves for specific costs or scenarios in the future. This has included more than $50 million per year in the FY 20 to 24 five-year plan as a reserve against reductions in federal funding. The City has also reserved funds for upcoming labor contracts and made a $34 million payment into the budget stabilization reserve fund, aka the rainy day fund. Also, the higher than anticipated ending fund balance in FY 19 enabled setting aside another $20 million into a recession reserve.

These reserves cushion us so that new costs or unexpected revenue losses don't immediately require service reductions and spending cuts. The improved fund balance has also allowed us to put additional money into the pension fund, which will help the fund get to full funding more quickly.

In a December 2019 report on the recession readiness of the 25 largest cities, rating agency Moody's acknowledged our progress, noting that Philadelphia like 17 other cities is moderately prepared for the next recession. Six cities were rated stronger and two were rated weak.

Moody's said that Philadelphia's better-prepared than it was in the last recession because we have begun building up of fund balance, we've made contributions to the rainy day fund and began the recession preparedness planning.

Despite this progress, when we evaluated the impact of different recession scenarios on Philadelphia this past fall, we found that on all but the mildest scenarios Philadelphia's current fund balance would not be enough. Moody's also highlighted our weaknesses, and our fund balance is a percent of revenues second worst, 24th out of 25 of the largest U.S. cities.

Despite the significant progress, Moody's recommends that Philadelphia grow its reserves and maintain fund balance percentages at levels equal with its peers which was 24.3 percent in 2007 going into the last recession and 32.4 percent in 2018.

They share that Philadelphia is the only city in the top 25 that didn't have an FY 18 fund balance that was larger than the decline in its fund balance during the last recession.

Philadelphia has made progress, but remains in a weaker fiscal health than we should be.

Next week on March 5th, Mayor Kenney will propose the Administration's FY 21 budget and FY 21 through 25 five-year financial plan. As with past plans and budgets, it will seek to balance the trade-offs between addressing immediate service demands and maintaining stable finances so that we can continue to meet the needs of Philadelphians in each year of the plan and beyond.

Even in an economic downturn, we look forward to working with City Council to continue improving Philadelphia's fiscal health. Thank you for the opportunity to testify this morning and I'm happy to answer any questions.

COUNCILMAN DOMB: Why don't we have all the testimony and then we'll come back to you with the questions. Rob?

MR. DUBOW: Oh, no --

MS. GOREN WAXMAN: That was it.

COUNCILMAN DOMB: Oh, you're not going to testify. All right. Councilmember Gilmore Richardson.

COUNCILWOMAN GILMORE RICHARDSON: Thank you, Mr. Chair. Thank you for your testimony. First, could you just break down for us the four different funds.

MS. GOREN WAXMAN: Certainly. First, we have the budget stabilization reserve or the rainy day fund. That is one that has a trigger having to do with the amount of revenues that come in and then a certain percentage getting to positive when there is enough revenue available, and that has sort of the strictest rules in terms of when money can come out.

So the very first payment ever came in during FY 20. That was $34 million. The current five-year plan anticipates deposits into the budget stabilization reserve throughout the current plan. The second reserve we have is the federal funds reserve. Starting in 2016 with the current presidential administration, the administration thought it was prudent to create a reserve against the potential for a lost federal funding, and that is funded over $50 million in each year of the current plan.

At the end of FY 19 given the larger than expected fund balance, we were able to deposit $20 million into a recession reserve. We are actually getting to sort of those last two, the federal funds reserve and the recession reserves, combine those and rebrand as a recession reserve to hedge against lost revenues, whether that's from federal sources, revenue sources, whether that's policy decisions or economic conditions.

And then the fourth is the labor reserve. As was mentioned during the last testimony, all four City contracts are expiring at the end of June and we expect there will be additional costs, so the current five-year plan includes $140 million anticipated against those increased labor costs going forward, so those are the four reserves we have.

COUNCILWOMAN GILMORE RICHARDSON: Thank you. Quickly, yesterday there was an article in the New York Times, CNN and a bunch of other publications around how the spread of the pandemic of the coronavirus has impacted our economy and increased fears for an economic downturn. Can you talk about our City's preparedness around that issue?

MS. GOREN WAXMAN: Certainly. And so, that's something that obviously us and the economists that the City consults with are looking at. And when we actually started our recession planning, obviously it's something that's always on our mind but November we started to really stress test.

And at that moment, it was an inverted yield curve and a trade war with China that we were concerned that that economic break with China would have an impact on us. Now, obviously those concerns have pivoted towards both the coronavirus and pandemic, whether that's a different economic break.

Different sources can have different impacts, but what we've been doing is trying to model sort of various levels of recession and what that means on our budget to try and figure out, okay, if it's small, medium or large, if it's short or it's long so that we can understand.

A lot of our goals, the last recession it was long, it was deep. Hopefully, the next recession doesn't have those characteristics, but a lot of what we're trying to do by building up these reserves is buy time so that we can have thoughtful responses. If it's a short recession, enough to get us through. If it does turn out to be longer and deeper, that we have some time so that we can make thoughtful decisions.

COUNCILWOMAN GILMORE RICHARDSON: Also, right now we're in the longest period of economic growth as an overall economy. And typically, when we project, the City projects the fund balances, it's a certain percentage of our obligations. So can you talk about why that is decreasing over time and not increasing?

MS. GOREN WAXMAN: So next week we will be coming out with the FY 21, FY 25 plan with a new set of fund balance projections. But really there's this constant trade-off for us. We understand that to really be prepared for a downturn in the future, we would want a higher fund balance.

The Government Finance Officers Association suggests 17 percent, two months of bills in the bank. And I think of the lady on WHYY telling you, you need six months of an emergency fund. But what we also realize is Philadelphia is a city with a lot of needs today, that for a lot of Philadelphians, it's already raining. And so, as we try and balance both of those two things together, that's where we're constantly having that push and pull about investing in services for vulnerable Philadelphians today as well as making sure we have them beforehand. And so, budgets are simply a series of trade-offs and those are the trade-offs that we have had to make over time.

COUNCILWOMAN GILMORE RICHARDSON: Sure. And also, could you just react to the report that was released yesterday relative to the quarterly overtime update?

MS. GOREN WAXMAN: Certainly. So yesterday we released a quarterly City managers report with each quarter. The Budget Office provides us a quarterly update that looks at our revenues, our spending, our performance across the City to figure out whether we're on track or off track.

And so, one of the things we do look at is overtime spending. So the most recent quarterly report did show that there was an increase compared to the same quota the prior year. It's about 13 percent of our overall spending on Class 100 are wages.

And actually, helpfully last quarter PICA did a really thoughtful analysis where they paired up the departments that had high vacancy rates and the larger overtime expenditures. And you can really see the interplay there. One of the things about being in a really good economy right now, it means that it is for some of our departments in some areas challenging to fill positions. And when we can't fill those positions with the services that need to be delivered, sometimes we need to rely on overtime.

The reason we do the

quarterly city managers report though is we want to make sure that we are making the most effective use of those overtime dollars as we can and really monitoring that. So we look at it each quarter as an area of concern, but we can see in some areas that there's certain economic pressures in trends so that our overall Class 100 spending is still on track, but the break between straight wages and overtime, that we see a shift.

COUNCILWOMAN GILMORE RICHARDSON: Thank you, Mr. Chair.

COUNCILMAN DOMB: Thank you, Councilmember. I have a few questions, but I want to recognize Councilmember Helen Gym has joined us. I have a few questions I just want to ask. First of all, congratulations on your position as Budget Director and I'm sure you're going to do a great job, so congratulations.

MS. GOREN WAXMAN: Thank you.

COUNCILMAN DOMB: Can you

tell us the kind of things that the Budget Office is doing to find savings across all departments?

MS. GOREN WAXMAN: Certainly. So as part of the annual budget process, in the beginning of December we asked all of the departments to basically say tell us what you need for the upcoming fiscal year, what more revenues do you need. But what we did this year also was ask for cut scenarios.

And what that means is we asked departments if you had to this year we said spend 3 percent or 5 percent less, what would you do. And part of that for us was recession-readiness planning because we wanted to make sure that if we do find ourselves in a recession and if it is sudden, that we are not surprised in making decisions on the fly, but that we have well-thought-out vetted plans.

But as part of that, there's also just that nice opportunity for reflections, so we're able to sit down with departments, have them evaluate, are there areas where they could be spending less, are there areas where they would shift, that maybe they would stop spending on this and start spending on that.

So we have those conversations with departments on an ongoing basis and found that some of them said, you know what, actually we identified areas where we don't need to spend this anymore and we would rather redirect it to that, so that's a constant process that we go through with departments while we're evaluating their budgets.

COUNCILMAN DOMB: Thank you. I have another question. The wage and BIRT tax are coming in over our original projections. And what's our projected fund balance looking like at the end of this year?

MS. GOREN WAXMAN: Certainly. This was last week when we released the

QCMR, we revised our FY 20 balance projection to be $352 million. That's an increase from the prior quarter. We had been at $307 million. However, still significantly below the $439 million that we were at last year, so we are sort of just getting there sort of meeting the low end of our 6 to 8 percent goal.

COUNCILMAN DOMB: And I'm not sure this is a question for you or for Rob. In the Road to 80, the pension, can you give us an idea where we are right now for funding?

MR. DUBOW: Sure. As you know, the Road to 80 pension had several components, all of which are actually in place now. One through negotiations with unions and partnership with Council. We got changes in both collecting bargaining agreements and what exempts and nonreps do for pensions. So contributions went up and the design of the plan changed so that it's a combination of defined benefit plan with a 401K plan. That's meant that assets have gone up because of the increased contributions and the growth and liabilities have started to slow because of the change in the design.

We've also put in more money from the sales tax. Remember, there was state legislation, moved some of the sales tax over to pensions. We've required that that be above the MMO, that state required amount that we put in. So all of that has helped with our funding. It's meant that last year for the first time in decades the pension fund was cash flow positive even without investment earnings, and it's meant that according to our actuary by the end of the current five-year plan, we'll be about 60 percent funded up from the mid-40s and that's with more conservative assumptions of things like earnings and mortality.

And when PEW looked at our pensions, they said that even if we miss our earnings assumptions, we'll continue to see improvements in our funding percent.

COUNCILMAN DOMB: I just want to make sure I understood. When is it going to be 60 percent funded?

MR. DUBOW: The end of the five-year plan period.

COUNCILMAN DOMB: In the five years from now?

MR. DUBOW: Yes.

COUNCILMAN DOMB: Okay. That's good news. Thank you. One last question, in the recent drop of interest rates that are dramatic, we focused on refinancing a lot of our debt that we could get more much attractive rates today.

MR. DUBOW: Yes, we've done a couple of things. We've done refunds across our credit so the General Fund -- we've also looked for any opportunity. We've also gotten out of some of our interest rate swaps to reduce our exposure to operate over time, so we've done both of those.

COUNCILMAN DOMB: That's good. Okay. Thank you. The Chair would like to recognize Councilmember Green.

COUNCILMAN GREEN: Thank you, Mr. Chair. Good morning to both of you. I just want to follow up with some questions based on some of the things that were stated and also, with the information provided.

Ms. Waxman, I'm curious in reference to, and I'm looking at this article from I'm not sure from -- oh, it's from PEW and it compares Philadelphia to a bunch of other cities, and I'm curious if you have any perspective on where we are from our rainy day fund dollars compared to cities like Detroit or Baltimore?

MS. GOREN WAXMAN: Off the top of my head, I'm not sure where they're at and sometimes it's not apples to oranges. One of the things I do know is Detroit actually has a much higher fund balance from us, but that's actually because their credit rating is so bad and they can't borrow money, so they need if they want to make those investments, to do that.

So there are times where having these super high fund balances of say Detroit, that actually indicates you've got other fiscal challenges that's sort of a point in time. So we do look at ourselves in terms of our peers but also trying to be mindful that sometimes there are different conditions on the ground.

COUNCILMAN GREEN: Okay. And that may be a question for the next speaker, especially I'm curious about Baltimore, Kansas City, Cincinnati and Cleveland in reference to where they are from a rainy day fund.

Some other questions, you talked earlier that we now have a recession reserve about $20 million and that's on top of the federal funding contingency fund. So we're looking at about $70 million?

MS. GOREN WAXMAN: Yes.

COUNCILMAN GREEN: I know the Mayor is going to give the budget address next week and we'll be seeing the new five-year plan for FY 21 through 25. Do you anticipate that same $70 million throughout the five-year plan?

MS. GOREN WAXMAN: I think we'll be able to talk more about the whole mix in balance of reserves. There'll be some changes across the four reserves that I mentioned before trying to be mindful of all the different needs that we have.

COUNCILMAN GREEN: But the goal is to try to extend it possible and maintain that level of that reserve fund, which includes both recessionary as well as what used to be the federal funding.

MS. GOREN WAXMAN: Yes. We're trying to balance both different roles. One is just our sort of plan vanilla fund balance in making sure that that's good. We also look at those recession reserves at the same time trying to balance that with our labor reserves and then the service needs and making sure that we're able to invest in services in our community, so we're sort of balancing all of those.

COUNCILMAN GREEN: And similar to the commentary I had for Mr. Rice when we're talking about PICA and independent fiscal office in future conversation, but once you revisit the questions I had for him for both of you regarding do you think that the trigger for the budget stabilization reserve for a rainy day fund should be changed as well?

MR. DUBOW: I don't know about whether the trigger should be changed. Do you think it would be helpful if there was a change so that we could make deposits in different times in the year? The way it's set up now, we can only do deposits when we're doing the budget. So I think that would a helpful change.

COUNCILMAN GREEN: So basically flexibility to be able to make deposits at different times based on what's happening from your projections versus actual numbers?

MS. GOREN WAXMAN: Yes.

MR. DUBOW: Yes.

COUNCILMAN GREEN: Mr. Dubow, you also talked a little about the pension. You and the Chair had a colloquy in reference to where we are from a pension funding balance that will be about 60 percent I believe.

MR. DUBOW: By the end of five years.

COUNCILMAN GREEN: by FY 25. You also said something earlier about the MMO or minimal municipal obligation and I want to make sure I heard you say that last year we actually put in more than an MMO?

MR. DUBOW: Yes. So we've

actually been funding the pension fund according to something called the revenue recognition policy, which is an amount that's higher than the state-required minimum useful obligation. So that MMO plus the contributions that employees agree to make during part of the last collecting bargain process plus the additional sales tax.

In addition, in the last couple of years when our fund balance comes in at a higher amount, we put in additional funding over those amounts into the pension fund.

COUNCILMAN GREEN: And was last year the first year that actually occurred or does that also occur in years prior?

MR. DUBOW: It happened the year before too.

COUNCILMAN GREEN: So in the last two fiscal years, we actually put in more than the MMO?

MR. DUBOW: More -- revenue

recognition policy we may have been doing for three years, but then we've put in amounts of both the revenue recognition policy for the last couple of years.

COUNCILMAN GREEN: Okay. Also, I just want to follow up on some back and forth that we had regarding overtime versus hiring. One of the things that occurred through a number of administrations is that, and I would say that you have to go back from the good administration on through, a number of administrations have not hired as much as people have left the City, and that's been a way of trying to address some of our budget constraints by not replacing people when they leave, and that caused our population, our census of employment to go down over time. And because of that perspective, the hiring, I think there's been a focus on not doing as much hiring and that's putting more of a pressure on overtime, which I think, Ms. Waxman, you talked about that tension.

Is there a way we can try to change that perspective? And I know now because we're -- that's been an unofficial policy for a period of time, but now we're in a very robust employment perspective. And so, that's caused an inability to hire because many more people are employed although we still have a high unemployment rate here in the City of Philadelphia, especially for people of color.

So I guess the question is how do we start to change that dynamic? I know we're going to labor contracts and that will also be part of that conversation, so I wanted to get a question on that.

MS. GOREN WAXMAN: So I think you sort of are noting that tension there about not wanting to hire, wanting to hire. And I think as you'll see as we move forward with the FY 21 to 25 plan, that we are putting an emphasis on trying to hire. There are certain areas where we are doing more to try and broaden the base of folks who sort of come into the hiring pool, reach out more broadly, particularly to reach out to communities of color, make sure that our recruitment is really robust and wide, but we know that there are certain areas that right now, particularly skilled trades, that we are having a very hard time simply because we can't commit in certain areas.

One of the things we already tried to do is push up the salaries in certain hard-to-fill areas so that we could attract more folks when we're really trying to get folks who might have other opportunities elsewhere. Also, the Chief Administrative Officer Office is working with OHR to figure out different ways how do we reduce the time to hire, how do we streamline that process, how do we make sure that also our retention is there, so that once people are on board with us they stay.

And so, there are a number of different opportunities where we're trying to bring folks on board and make sure that is an inclusive and successful process. Then we'll be able to talk more about that throughout the budget process.

COUNCILMAN GREEN: We are going through on the precipice of what many people are calling a Silver Tsunami where in a number of industries, employment sectors you have a significant wave of people as my father would say, seasoned employees that will be leaving the workforce. And so, that's going to have additional pressures on our ability to address this overtime versus hiring dynamic.

I wanted to also ask you, you talked about the budget process which ever year the Budget Office reaches out to various departments to provide their budgets for the year. And although we are in a better economic situation than we've been in for a number of years, you still requested those various departments to provide data on what it would look like if they had a 3 percent reduction.

I think that's actually a good idea to start to do that and not only do it in a recessionary context, but there's been conversation over the years about 0 based budgeting, and it's been stops and starts in that regard. Can you give some perspective on how we get to that concept and does this initiative you started as Budget Director help us to move in that path?

MS. GOREN WAXMAN: And I will say that I'm not the first budget director to ask for cuts and --

COUNCILMAN GREEN: Well, let me just correct the record. I know Mr. Dubow has done that as well, but often we've had to do that because we were facing very significant financial perspectives. This is one of the first times that I remember hearing that you've asked departments to make those presentations on reductions when we have not been in such dire straits.

MS. GOREN WAXMAN: To not make me super popular. Right now the City uses program-based budgeting which is really focused on tying performance with the budget, but also making sure that you understand every bit of that. I think that there really is a bridge between that 0 based budgeting, the program based budgeting, because when you start looking at a department's spending and breaking it down into meaningful chunks that are actual services, we deliver, this is the sanitation program, this is what we put into inspecting restaurants. That gives you that opportunity to figure out, okay, this is the level of service we're providing, is it not enough, too much, just the right size.

And so, going through those cut scenarios, one of the ways that we asked departments to think about this and we asked for a 3 percent to 5 percent, 3 percent said it's fine sort of if you want to look at those incremental reductions, if you want to snip a little here, snip a little there.

But when looking at those 5 percents, we asked them to think more about are there lines of service that you would discontinue, that maybe instead of a scenario where you do five things not nearly up to snuff, would you want to look at doing four things but doing them all really well, so that creates that opportunity to sort of think in both frameworks, both the incremental cuts as well as changing just sort of generally what services we provide.

And part of the thought process around that is thinking about, say, we were to go into a recession, if it is long and deep, you might really need to think about what services do we as a city provide. If it's short, we're looking to just sort of get through until we get back to normal, then maybe you don't need to have those conversations so we're trying to have both. So I think that second area, the deeper in thinking through what do we do and not do gets closer to that 0 based budgeting. The other is more of that incremental approach, and we really like to on both of those approaches think about what does that mean for service delivery, so that if we were to cut your dollars here or if you had less resources to do X, what does that mean in terms of days to process whatever or how long we're or how many services we can provide.

COUNCILMAN GREEN: One final question, and prior to the influx of the coronavirus and some of the --

MS. GOREN WAXMAN: I promise I don't have that. I've been to the doctor's.

COUNCILMAN GREEN: Okay. I don't have my mask with me either, but

I don't know how much my mask will cover me. Now, prior to the influx of the coronavirus and also some of the concerns regarding trade and tariff wars with China, most economists project a very low possibility of a recession in this year going into next year. That may change.

But based on the conversations we've had today and even with a possibility of even a future recession, most economists have said that that recession will not nearly be as challenging as the prior recession we came out of a couple of years ago. It will be quicker, not as impactful.

However, we have, for a lack of a better word, a School District recession on the horizon. I had asked the question to Harvey Rice about his concerns regarding the financial conditions of the School District, especially now that we have local control and we look at that issue, plus labor contracts that we're currently negotiating now and also the need to have a better fund balance based on a number of indicators that we need as well as trying to maintain the reserve and federal funding contingency. What are your thoughts on that going forward?

MS. GOREN WAXMAN: So the current five-year plan includes a historic level of funding from the City to the School District, over $1.2 billion. And your question really gets to the heart of those trade-offs we're trying to constantly balance the immediate needs. We believe our School District has immediate needs with making sure that we also have reserve so that we can continue to provide services this year throughout the five-year plan come what may in the economy. And so, that is something that we carefully look at as we develop the budget and the five-year plan in talking with the School District to understand what their needs are.

COUNCILMAN GREEN: Mr. Dubow?

MS. DUBOW: I think that what you've gone through is a really good way of highlighting all the challenges we face as we attempt, one, to put the plan together and, two, to prepare for a recession. All of those are major issues and that's what we're grappling with as we try to put a plan together for next week.

COUNCILMAN GREEN: Okay. So we'll look to see your thoughts in next week's budget address and the five-year plan for FY 21 to 25. Thank you, Mr. Chair.

COUNCILMAN DOMB: Thank you, Councilmember Green. And the Chair would like to recognize Councilman Gym.

COUNCILWOMAN GYM: Thank you very much, Mr. Chairman. I appreciate it. So I'm going to just continue along with the line of questioning that Councilmember Green had asked about the schools.

MR. DUBOW: I thought you

might.

COUNCILWOMAN GYM: I'm sorry?

MR. DUBOW: I thought you might.

COUNCILWOMAN GYM: So we got rid of the MOU, which allowed a continuation maintenance of effort agreement between --

MR. DUBOW: Correct.

COUNCILWOMAN GYM: -- I should have said an MOE, maintenance of effort agreement between the School District and the City of Philadelphia. At the time, it made a lot of sense, particularly during the years in which I think what we found is that the School District in my opinion seemed to see like a lagging indication from the impact of the recession. So while the recession may have hit most City businesses during I think my colleague would have said maybe between the years of 2008 to 2011, the District's devastating budget through the state really hit between 2012. We closed down 24 public schools in January of 2013, September of 2013 opened with 4,000 less staff, schools closed and then that continued through until we started reversing that most recently in 2016 and 2017.

So have you thought about how -- I know that there's going to need to be ongoing dialogue and I do think that we need to make sure that the School District itself is included, but have you thought about the impact of a recession plus a lagging or potential for a lagging kind of impact on one of the most significant entities that cannot raise its own money unfortunately, relies heavily and probably too much so but increasingly more on local funding, what that may look like because it actually in my opinion drags out the length of time that we might have?

I'd also be curious if you agree that you think that the District somewhat lagged whereas we saw investments continue at a marginal rate, certainly not robustly, but not the kinds of severe cuts that we saw that really frankly devastated a lot of the communities, had tremendous impact on children and neighborhoods across the City?

MR. DUBOW: So the School District definitely lagged last time. I think part of the reason for the lag was the influx, the stimulus money that the District used to make investments and to hire staff. And I think the big hit they took was when that stimulus money went away and the new governor said not to try to replace those funds. So I'm not sure that in a new recession that they would lag again. I think that they might take a hit fairly quickly as we would, which makes planning with them, as you're saying even more important.

COUNCILWOMAN GYM: Yes. Okay. And then do you have opinions about where you would be on maintenance of effort should that be a situation in which, you know, like again the District cannot raise its own funds? A lot of our delivery to the District is delivered through grants so it's not necessarily through, like it's relatively -- we're committed obviously. They have a five-year plan. We have a five-year plan. On the other hand, it is somewhat discretionary because it's given through a grant process as opposed to property tax delivery or something that's formula-based as opposed to negotiated.

MR. DUBOW: So probably the state should be the prime funder and the City should provide reliable funding to the District and together, that should be a significant amount of funding for the District to provide the services it needs to provide.

I think the maintenance of effort was kind of a plus and a minus. It was a plus in that it gave the District some security that they knew that the City funding wouldn't go down. On the other hand, it made us much more cautious about providing funding to the District, something for example as a one-time thing, it was much harder to do that because you couldn't give -- if you wanted to give $50 million for a specific item, the issue is how do you get around the maintenance of effort. And so, it was actually in some cases a bar to giving money to the District. So I'm not sure that it would actually help the District in the long run as much as the City and the state living up to the commitments.

COUNCILWOMAN GYM: I think one of the questions would be that I think that the ability to do large-scale grants at different points in time, like, for example, if we wanted to fund a big school's investment, for example, that might sunset at some different point in time down the road, is a much different financial scenario.

I am curious about where you would be somewhat on a maintenance of effort through a recessionary period, because actually you don't really -- I think what the District has consistently said to us about its problems, particularly with the state and with the federal government which can withdraw money actually, because again, a lot of the District's money is dependent upon grants and negotiated delivery as opposed to do right, which is really what we should be moving towards.

I think what we heard repeatedly from them was that stability and predictability is their main interest, even when that may not be incredibly generous. But that in times of downturn, an economic downturn, stability and predictability are more important than whether or not they can get like a sort of, I don't know, I wouldn't call it a windfall, but like a break in case something goes horrifically bad.

MR. DUBOW: Right. I can completely hear what you're saying and I would not want us to reduce funding to the District in a recession because then we're just kind of doubling down on their problems. I think our putting money in each year of the five-year plan gives them some stability because they can see what we're planning to do. So the combination of -- in some ways, that gives them some assurance that they'll get that money regardless of what happens in the economy whereas the property tax, income tax, those can all go down and will go down when the economy turns. Our giving them a contribution actually kind is a steady state of funding.

COUNCILWOMAN GYM: Do you think the current relationship with the District is strong enough to have good stable, predictable, reliable conversations about the District's financial path?

MR. DUBOW: I think it is. We have regular meetings with the CFO of the School District. We go to their financing and facilities committee meetings. There are regular discussions between the School District's Chief of Staff, the Mayor's Chief of Staff, between the Superintendent and the Mayor and between the Board and the Mayor's Office so there's a lot of dialogue. I think the relationship is very strong.

COUNCILWOMAN GYM: And you think they've been accurate, for example, about predicting facilities conditions or the need for facilities, they have a good assessment on terms of infrastructure and the fact that 10 schools closed this year, for example?

MR. DUBOW: Yeah. So --

COUNCILWOMAN GYM: Since September.

MR. DUBOW: Obviously, any large organization has challenges but that's different from our having a good working relationship with them on their operations and their finances.

COUNCILWOMAN GYM: Yes. 10 schools did close down since September, though.

MR. DUBOW: Yes.

COUNCILWOMAN GYM: And one last question, and congratulations on your new position as Budget Director.

MS. GOREN WAXMAN: Thank you.

COUNCILWOMAN GYM: When we give out City grants or subsidies, traditionally they might be delivered through the Commerce Department and others, and we've done legislation that requests that there's some feedback on subsidies when it's specifically related to job growth, job development, that kind of thing.

Does anyone ever do any evaluation of economic subsidy grants in terms of how they contribute back to budget revenues or to tax revenue or growth and overall? Is that your department that actually does that?

MR. GOREN WAXMAN: So what I would say is actually there was somewhat recent legislation that put in place looking at job incentives. And so, the Commerce Department took the lead but with help from the Revenue Department, the Budget Office, the Finance Office doing an evaluation starting with some of the incentive and subsidy programs for when businesses are granted funds.

So they completed an analysis and delivered recommendations on a number of programs, so it's sort a rolling basis so that different programs will get evaluated each year. And that's actually what then led to the inclusive growth strategy that was released by the Department of Commerce talking about how we could pivot, make some adjustments based on how our current sort of suite of programs were performing against sort of expectations and job growth, but also in terms of inclusivity and other factors and also compared to what the market was for incentives from other jurisdictions.

COUNCILWOMAN GYM: And just to be clear, that also includes revenue --

MS. GOREN WAXMAN: Sorry.

COUNCILWOMAN GYM: That's okay. Do you need more water?

MS. GOREN WAXMAN: I'm fine.

COUNCILWOMAN GYM: Revenue and that also includes just revenue and overall tax payments like defaults, that kind of thing with the entities that receive the subsidies. Is that accurate, you'll consider that as part of that --

MS. GOREN WAXMAN: Yeah, so that was part of the analysis.

COUNCILWOMAN GYM: Because sometimes it's just limited to jobs and I want to make sure that --

MS. GOREN WAXMAN: Sure. So what they would be looking at is sort of the ROI, on those incentives, is one of the things they analyzed. They used an outside firm who had done this for a number of different cities. And so, that factored into that analysis.

COUNCILWOMAN GYM: And then do you internally do that within revenue or is this mostly outsourced, that analysis?

MS. GOREN WAXMAN: So different programs, it varies --

MR. DUBOW: You can take a rest.

MS. GOREN WAXMAN: Okay, yes. Thank you.

MR. DUBOW: It's a combination. So sometimes it's outside firms. Sometimes it's our Revenue Department and any department working in combination with Commerce and Budget, so it really varies by analysis.

COUNCILWOMAN GYM: All right. Thank you very much.

COUNCILMAN DOMB: Thank you, Councilmember Gym. I have one comment. Just let me hear your thoughts on it and, that is, I know that we have a very, very large percentage of our economy that's eds and meds, educational institutions and medical institutions. And while they're in boom time, they're always complaining they don't pay real estate taxes or business taxes. In downturns, thank God we have them because they are very stable in our economy, very stable. So we don't have the big downs as other cities do.

And now with even the cell therapy that the University of Penn is doing, the tremendous cell therapy, I actually think in my opinion that if we experience a downturn in Philadelphia, it may not be as severe as it will be in other areas, which I think is a positive. I'd just like to hear your thoughts on that.

MS. GOREN WAXMAN: So one of the things that we did with our stress testing in the late fall was actually look back to the past three recessions and look by tax type. And one of the things we found was our wage tax which with our very large eds and meds sector even in the last recession, which was the largest of the three we looked at in terms of depth and length, our wage tax receipts were paused as opposed to declined, and that was a really interesting finding I think that speaks to what you're talking about whereas our tax types that are on for-profit businesses, particularly the net income portion of the BIRT saw tremendous amount of volatility. And then there's some tax types that are more volatile based on the market that is sort of a mix of the nonprofit and the for-profit, our realty transfer tax. And so, we do see that there is a certain steadiness in -- there's an interplay. We've in part got the economic sort of make-up we have because of the tax structure we have and vice versa and an interplay there that the wage taxes are a number one tax source and that captures the for- and nonprofit sectors.

COUNCILMAN DOMB: I think that's a very interesting fact that you brought up, that the wage tax stays steady basically in a downturn. That's very, very comforting, very important for us to know so thank you.

MR. DUBOW: Yes. Really where we saw in the last recession, the first hits were in the BIRT and the transfer tax and a little bit in the sales tax, but not as much in the wage tax.

COUNCILMAN DOMB: That's good. Okay. The Chair would like to recognize Councilmember Gilmore Richardson.

COUNCILWOMAN GILMORE RICHARDSON: Yes. Thank you, Mr. Chair, and thank you all for your testimony again. I just have a very quick question relative to our municipal budgeting model. I believe this is our first year moving all of our City departments to program-based budgeting, correct?

MS. GOREN WAXMAN: All the mayoral agencies are now doing program-based budgeting. It's been sort of a four-year roll-out to get folks in. So some departments it's year 4. For some, it's year 1.

COUNCILWOMAN GILMORE RICHARDSON: Sure. So in my studies and in grad school and I applied to a PH.D. program around program-based budgeting in different municipal-budgeting models, so it is an interest area of mine. Typically, after year 3 or 4, you have realized savings and your change in the budgeting model, have we seen any realized savings as we changed our municipal-budgeting model in the City?

MS. GOREN WAXMAN: I think that one of the things that it has really allowed us to do is figure out where we want to direct those resources. Unfortunately, Philadelphia, our needs are still up here and our resources are down here.

And so, what it lets us do is sort of figure out where we're getting the biggest bang for our buck. So one the I would say success stories that we've really seen through program-based budgeting was the Health Department came and showed up, you know, it's a really long lag. I think it was up to 17 or 18 months between restaurant inspections and to make sure that Philadelphia residents and visitors are eating in healthy and clean establishments, they really wanted to get to a much shorter window.

And what they were able to say was, if you give us X amount of dollars, we're going to translate that into resources and we'll be able to show you through this measure that now we're actually getting to their goal. They set themselves with 12 months and actually with those extra resources, they were able to start a rotation where they were getting on average every 11 months.

And so, what the program based-budgeting is really allowing us to do is make sure when we're investigating dollars, we're getting results. So it's less about figuring out where we've been spending too much, but figuring out where we can spend to get the biggest impact.

COUNCILWOMAN GILMORE RICHARDSON: Okay. So more on service, delivery and improving our service delivery to citizens?

MS. GOREN WAXMAN: Um-hmm.

COUNCILWOMAN GILMORE RICHARDSON: Quickly around the increase in pay and your capital spending, now with our interest rates being at a historic low and thinking about our capital needs over time, have you all been having discussions around how we're planning our capital needs relative to what we're able to do based on the funds that we have now? And then if and when something occurs, the interest rate would obviously go up. How are we planning for that relative to our capital needs?

MS. GOREN WAXMAN: So we try and be very thoughtful understanding, one, what would our infrastructure need, and we are an old city. We are a city built for a lot more people than currently live here. There's a lot to maintain and we know that putting those investments in existing and new facilities, the need is here.

One of the things we've been doing is we do our capital program, is actually a six-year program, so similar to the five-year plan. We do try to be strategic in terms of understanding, first of all, what dollars we can put in without actually having to borrow.

And so, one of the things we were able to do during the last year transfer ordinance process was allocate $47 million for pay-as-you-go capital investments. And so, what that does for us is, one, it lets us address needs that were unmet, that clearly there are needs that are unmet. Also, other things it lets us sort of avoid borrowing for certain things that we've been planning to in the coming year.

And so, that helps us reduce our costs because high interest rate, low interest rate, no interest rate is even better. So that's where we're putting a lot of our attention.

And in terms of looking forward, we look a lot at that interplay between the capital program, how much we're borrowing and what that does to our debt service in the operating budget. Because as we mentioned earlier in the testimony, that between our debit service and our pension obligations, that's 20 percent of our budget so we're constantly trying to be mindful that we not squeeze out the funds available for day-to-day service delivery by locking ourselves into those fixed costs. So we're constantly balancing the two.

And right now a lot of our focus has been on when we can doing that pay-as-you-go capital financing. Another thing to mention about interest rates and what we do, the market is going to have interest rates change but the control we do have is doing what we can to try and improve our credit rating.

And so, the Treasure's Office was able to share with me that right now our credit rating is A, which is if we were one rung below that, it would be BBB, right now the difference on $100 million borrowing and our interest would be $332,000.

If we were able to get our credit rating up to an AAA, the strongest there is, we would save $690,000 compared to if we were at that BBB level. So being able to improve our fiscal condition, improve our credit rating saves us money.

And the second thing that I

haven't gotten to mention yet but I'm really just going to share with you --

MR. DUBOW: Can I share one thing about the --

MS. GOREN WAXMAN: Yes.

MR. DUBOW: So the other thing in the way our bonds have been selling, not only have they been selling better because we're rated better, they've been selling better compared to the standard benchmarks for other jurisdictions rated at our rating, so we're actually trading even better than AA, and I think part of that is because of what the market sees us doing with our fund balances, what they see us doing with our pensions so they like the progress we're making and that kind of translates into better results when we go to markets.

MS. GOREN WAXMAN: And the thing I want to add onto that is the other thing, in the past two years the City of Philadelphia was able to avoid doing a tax revenue anticipation note, which in periods of time where we didn't have enough cash on hand to pay bills early in the year before those real estate receipts and BIRT receipts, we would have to borrow money. From the '70s until 2018, we had to do those tax revenue anticipation notes every year but for one.

The past two years we didn't have to do that. We had enough cash on hand that we were able to make it through. What that did was in terms of the interest savings, the straight up borrowing cost saves us $2.3 million. That was the average cost of doing that. The four years before, we were able to not do that.

So being physically responsible, that really does free up cash today. So those are the sorts of trade-offs. And by paying attention to our fiscal help really does make sure that we can address all of the needs of Philadelphians on the service side.

MR. DUBOW: And in 10 years

we've gone from having to meet weekly, whether there were vendors that we had to delay paying because cash was so weak, to not having to do cash flow borrowings.

COUNCILWOMAN GILMORE RICHARDSON: And just really quickly, I wanted to follow up on the line of questioning from my colleague Councilmember Gym relative to the School District. How were you thoughtful in the planning of this upcoming budget around the increase, not only capital, but really operating expenses the District has incurred relative to the lead and asbestos issues that have been happening in the District?

Do you give any consideration to that in your planning and could you just talk about that?

MR. DUBOW: Yes. And part of our ongoing conversations with the District are about their projections for their needs and how they want to handle things like facilities in their budget and then how that reflects back to what we need to do, so that's definitely been part of our conversations with them.

COUNCILWOMAN GILMORE RICHARDSON: Okay. Thank you. Thank you, Mr. Chair.

COUNCILMAN DOMB: Thank you, Councilmember. Thank you for your testimony today. And you should have some chicken soup, Marisa. But thank you very much. Thank you, Rob. Will the Clerk please call the next panel?

THE CLERK: Tom Ginsberg.

(Witness approached Witness Table.)

COUNCILMAN DOMB: Good morning.

MR. GINSBERG: Good morning.

COUNCILMAN DOMB: Please state your full name for the record and proceed with your testimony.

MR. GINSBERG: Thank you for

the opportunity to testify today. My name is Thomas Ginsberg. I'm a Senior Officer at the PEW Charitable Trusts Philadelphia research and policy initiative. We're a project that produces analyses of key issues and engages with decision-makers on policies.

PEW has done extensive research on the fiscal tool that we've talked about today, rainy day fund known here as the budget stabilization reserve fund, which along with other budgetary control actions is a useful way for coping with and sometimes taking advantage of volatility in government revenues that often followed swings in the economy and the tax base, both up and down.

Governments use rainy day funds to help ensure that they can keep providing essential services in shouldering liabilities if or when their revenues fall after an extreme event or an economic slump. This starts with putting away a certain prescribed amount into a dedicated reserve during good times, and that involves picking the optimum formula in the timing of the deposit.

Our research has found that Philadelphia is one of 18 major U.S. cities that currently use this tool in one form or another. New York City actually is the latest to consider joining this group of cities. We at PEW held an event on the topic in October 2018.

At that event, an official from Los Angeles said that he sees his city's rainy day fund as one part of a tool kit for fiscal policy. He said, "We don't want to be in crisis management in the next downturn. We want as many tools as possible for when times are not as good as they are now."

There's a lot to learn on this subject from state governments, where rainy day funds are much more common than in cities. 48 states including Pennsylvania currently have a dedicated economic reserve fund of some kind.

Our researchers found that there are some common elements in those state funds, common elements of well-designed funds. What we found is that well-designed funds codified in law, that they are institutionalized with clear goals such as protection from a downturn and that's important to getting the most benefit from it.

When the rules and goals are enshrined in law or formal procedures, they have a better chance of remaining on course through changes in the elected leadership and budget priorities, and they are transparent for rating agencies and the public. And Philadelphia can check this box. Its fund is codified in the City Charter.

Deposits, they should be tied to revenue volatility, that is, governments should set up their funds to take advantage of growth and revenue that may not be sustainable otherwise or may be a one-time spike. Philadelphia currently deposits a defined amount based on projected year-end budget surplus, not so much revenue.

While this type of rule sometimes works, the research shows in states generally that it does not consistently track closely to actual revenues or economic trends that the City may be experiencing. The amount of money in the fund also matters. Philadelphia's rainy day fund currently holds about $34.3 million. It was created in 2011 by a ballot measure and sat empty for seven years.

In 2019 after several years of revenue growth, the Kenney Administration using those rules, the same rules that were laid out in the Charter, made the first deposit. Like other cities, Philadelphia has also other reserves you've talked about here today set up for various purposes. On withdrawals, the experience of states show the importance of clear rules on withdrawals. Officials should withdraw money only when the indicators related to their goals show that the time is right, such as a measure of economic slow-down or declines in revenue and they should stop withdrawals when those measures show that the economic conditions and revenue volatility has actually improved.

In Philadelphia, the withdrawal rules in the Charter are pegged to revenues as well as expenditures. They state that the City can make withdrawals when actual prior revenues came in at least 1 percent below the year's official projections or when necessary in the current year to pay for emergency services or to avoid material disruption services.

So aside from all of those elements, having a codified purpose and having effective deposit and withdrawal rules, there is a key benefit of having a well-defined rainy day fund and, that is, credit agencies look at them when judging a government's fiscal condition.

Our researchers found that agencies tend to look favorably on governments that strictly follow their rules both for deposits and withdrawals. In fact, the leading agencies, everything else equal usually do not penalize the government for taking money out of a rainy day fund during downturns as long as they do in accordance with the rules that they set out. In other words, both depositing and withdrawing under the rules can be a credit positive.

As one analyst said during our event, if you have a reserve policy and you're not implementing it, it's not a strengthening factor for you. Thank you very much for your time and attention and I'm happy to address any questions I can.

COUNCILMAN DOMB: Thank you for your testimony.

MR. GINSBERG: Thank you.

COUNCILMAN DOMB: I have a few questions I wanted to ask. Are you suggesting one of two things, either we build it into our budget a certain percentage of our gross revenue goes into a reserve fund every year no matter what and/or are you suggesting that above the budgeted amount of revenue, we take a percentage of that and put it into the reserve?

MR. GINSBERG: Well, I don't mean to be suggesting a particular formula. I'm just making the point that we found in our research, that the states that have had rainy day funds for years, they started out with the kind of formula that Philadelphia has now, which is measuring your budget surplus and using that as an indicator of how much you take out.

States have shifted over the years to more of a strictly revenue-side analysis and now looking at the revenue volatility and using perhaps an average of past years' cases, instances where actual revenue came in above projected revenue apart from whatever the budget says.

And when you focus on that side of it, then you get a measure of a more -- tend to get a more accurate review of what's happening in the economy and your tax base. So the specific percentage that's up to each state. Each government sets through its own process.

COUNCILMAN DOMB: Chair would like to recognize Councilmember Gilmore Richardson.

COUNCILWOMAN GILMORE RICHARDSON: Thank you. Thank you so much for your testimony. And I just wanted to go back to your testimony where you talked about deposits as well. Philadelphia currently deposits a defined amount based on projected year-end budget surplus.

Can you talk about some other municipalities and/or states that utilize the other format where they make contributions throughout the year based on the actual numbers that come in?

MR. GINSBERG: Some of our research has looked at Utah, Texas I believe has adopted this sort of process. Now, economies are different in those places too of course and those are state-wide systems rather than our city-wide. But as I said, I think around -- I'm sorry. I'm doing this from memory a little bit. Out of the 48 states, a fair number now have moved over to revenue rules.

I could get you the exact list of states that actually do that. And actually just last week ahead of this hearing, we decided to start looking deeper at what cities do in that regard also, so we will dig into that and I'll let you know.

COUNCILWOMAN GILMORE

RICHARDSON: Okay. Thank you so much. That will be most helpful. Thank you.

COUNCILMAN DOMB: I have another question for you actually. Hearing the Budget Director's testimony about the wage taxes in the prior recessions, that they were basically flat which I thought was very positive versus going down. I thought that was a great indicator of our economy in a downward recession.

Have we looked at other cities to see any other indicators they've lost further than Philadelphia so that we can say we're actually in a better position to weather a downturn?

MR. GINSBERG: Well, there are a few things that happened in the economy that happens to the tax base, and some taxes are more exposed to what happens in economy than other obviously. Generally speaking, and I can't speak to exactly the comments about the City's wage tax. Generally speaking, income taxes are more susceptible to movement with economy than say property taxes, which tend to be much more stable with ups and downs.

And some of our analysis has looked at again the state level and we haven't done as much at the City level, but it goes to my point about revenue volatility. Revenue volatility can be measured and tends to be -- revenues tend to be more volatile when an area is more dependent on income-type taxes rather than property taxes or some other stable source.

Now, what was happening specifically in the health care sector here, which is our biggest sector, it's hard to know. There are a lot of other things in that sector that would affect the wage taxes going up and down. By its nature, it's a more stable industry than pick almost any other. So there might have been a lot of things going on there.

I can just tell you that our research has shown revenue volatility is higher in places that are more dependent on income-type taxes.

COUNCILMAN DOMB: In your opinion, we heard the Administration saying we're shooting to 8 to 9 percent in reserves, but I guess the accounting professionals are saying that we should be looking closer to 17 percent. What's your opinion on those two different numbers?

MR. GINSBERG: So I don't have an opinion particularly on that. The association, the GFOA, that sets that 17 percent has been setting that for quite a while and they've looked at it over the years and I will just defer to them. It's not the kind of research that we do.

COUNCILMAN DOMB: All right. But in simpler terms what they're saying I guess is we have one month reserves versus two month's reserves.

MR. GINSBERG: That's the way the GFOA usually phrases it. They can express it either as a percentage, but it's what is often they've said they found more useful to express it in how many days of funding do you have for your expenditures.

COUNCILMAN DOMB: Okay. Well, thank you very much for your testimony. Thank you.

MR. GINSBERG: Thank you.

COUNCILMAN DOMB: This concludes the hearing on Resolution 200039. And I want to thank everybody for participating and I want to thank the sponsor for bringing this forward. Thank you very much. Thank you.

COUNCILWOMAN GILMORE RICHARDSON: Thank you.

(Committee on Fiscal Stability and Intergovernmental Cooperation concluded at 11:45 a.m.)

C E R T I F I C A T I O N

I, hereby certify that the proceedings and evidence noted are contained fully and accurately in the stenographic notes taken by me in the foregoing matter, and this is a correct transcript of the same.

____
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