APPENDIX A:

BLUE RIBBON COMMITTEE

SUB-COMMITTEE REPORTS

ALLENTOWN
PENNSYLVANIA

Allentown Blue Ribbon Committee – Expense Sub-Committee Recommendations

The Present Model is Not Sustainable and a Paradigm Shift is Necessary

June 2009

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Overview

The Expense Sub-Committee, herein after referred to as (Committee) was tasked with developing both short and long term high level strategies to help the City of Allentown control and reduce expenses within the context of providing appropriate municipal services.

From the outset, the Committee decided not to focus on small dollar amounts or solely on short term solutions. Rather, the Committee felt that focusing on long term sustainable solutions that would allow the City to move toward a strong financial model built on the foundation of prudent budget and management practices, using benchmarking and detailed analysis, would yield greater value, and would ensure a balanced budget without the need to employ the fund balance.

The Committee felt strongly that in order to move to a sustainable financing model, the City must act boldly with its stakeholders to implement these recommendations. Failure to act on some of the larger, long term/structural recommendations will lead to the continuing need to look for short term solutions for years to come. Sustainable change does not come easily but it is required. **The present model is not sustainable and a paradigm shift is necessary.**

Questions relating to this report should be directed to the Committee chairperson, Deana Zosky, at dmzeverg@ptd.net or 484-951-1289.

Executive Summary

A recent PEW Trust Report titled **Tough Decisions and Limited Options: How Philadelphia and Other Cities are Balancing Budgets in a Time of Recession** discusses the challenges being faced and the choices being made by other cities across the country. (See www.pewtrusts.org/philaresearch for the full report) Many of the recommendations that are being put forth by this Committee are the same or very similar to those being considered by these other major cities.

A few excerpts from the report set the tenor (though not necessarily the particulars) of what a full discussion of the paradigm shift for Allentown must contain:

> *All over America, cities are grappling with budget problems brought on by the financial crisis and the recession. Falling revenues and weakened pension funds have combined to force City officials to make extremely tough choices.*
>
> *Still, choices have to be made, and cities are making them.*
>
> *Rather than increase broad-based taxes, most of the cities studied in this report are emphasizing cutting services and coupling those cuts with furloughs, workforce reductions, freezes on salaries and demands for wage and benefit concessions from municipal labor unions.*
>
> *Every situation is different. But each City has to balance its budget by using two basic tools: reducing expenditures and raising revenues. Neither is easy. Eliminating services can spark public outcry: witness the protests over proposed library closures in Philadelphia last fall. Efforts to make government more efficient are difficult to quantify and may take years to materialize. Trimming the cost of services usually means cutting personnel costs, which frequently requires the consent of municipal labor unions.*
>
> *For the most part, proposed service cuts are targeting libraries, recreation facilities and aspects of trash collection. In a number of places, fire departments are shrinking.*

Personnel costs make up the largest percentage of any City's budget. To reduce personnel costs, cities must shrink the size of their workforce and/or cut their per-employee costs.

Tough Decisions and Limited Options: How Philadelphia and Other Cities are Balancing Budgets in a Time of Recession Claire Shubik, May 2009

Given that current revenue sources will not be able to keep up with the expected growth of expenses, this Committee recommends the following broad categories for review and action:

Salaries and Benefits. Given that 77% of the City's budget is consumed by these two items, significant attention must be given to this. While the specifics are detailed in the body of this report, generally the concept is that all labor contracts should be examined and significant changes made to bring them into compliance with current market conditions as it pertains to the cities costs. In addition, opt out programs and early retirement options should be explored.

Best Practices/Benchmarking. While acknowledging that the City is both implementing and contemplating a number of Best Practices, it is the recommendation of the Committee that a mindset of benchmarking and utilization of ONLY Best Practices become the norm, such as best practices in private business and not-for profit and public practices of the International City Managers Association (ICMA).

Rightsizing. Many opportunities for savings may be found by rightsizing or using a shared service center approach for different functions, either to privatized sources or multi-jurisdictional consortiums.

Sale and/or Development of New Tax Parcels. While not technically an expense consideration, the Committee felt strongly that development of current non-taxed parcels of land could generate significant tax revenues, as well as avoid certain ongoing costs.

Detailed Recommendations

Benefits

1. **Analysis and Benchmarking**. Given that approximately 77% of the City budget is spent on personnel and benefits, all potential savings items relating to these specific expenses must be thoroughly analyzed and vigorously pursued based on dollar impact. A detailed historical analysis of all of the benefit components and benchmarking in and out of business sector for 5 or more years should be completed which would include the costs of all types of benefits and compared to other municipalities and companies as a means determining comparable benefit structure. The City should also perform benchmarking of comparable cities and companies as it relates to staffing levels to ensure that structural changes are made to move to a more sustainable model. Analysis of vacation, sick and holiday policies and benefit impact should be included and could be compared to hours worked or hours paid.
2. **Opt Out Program.** The City should analyze the amount needed to offer an aggressive opt-out program for medical and other benefits that would provide long term net cost avoidance benefits. Currently, the opt-out program is voluntary and with no compensation and as such offers little incentive not to accept benefits. For example, Lehigh County offers an opt-out of $780 per year for employees who choose not to have the organization cover their health care and presently 9% of their employees have opted-out.
3. **Health Care Contribution and Co-payment.** The City should consider instituting a mandatory and substantial, either phased in or one time structural change, employee benefit contribution for co-payment and cost sharing of all employees receiving benefits based on benchmarking results. Typically, companies now require between 10-30% of the cost sharing or co-payment requirement to help reduce the burden of increased health care. Presently, the City requires minimal contributions of any kind to help defray escalating benefits costs. Lehigh County employees contribute approximately 15%.
4. **Post Retirement Healthcare.** The City should consider renegotiation of all labor contracts to terminate post retirement health care by analyzing the feasibility of either a termination date for all post-retirement benefits after a certain year or the creation of a union-managed independent trust, known as a Voluntary Employee Benefit Association (VEBA) which would permanently assume the sole obligation of retiree health benefits to current and future retirees, spouses, survivors and their dependents. This would eliminate any future health care liability on the part of the City for post retirement health care. Lehigh County has not provided post retirement healthcare to it employees starting after 1987, saving the county a substantial amount of money.
5. **Insurance Policy Review.** The City should perform a comprehensive review of personal insurance policies (health, dental, prescription, and life) to look at whether to continue the benefit and pursue savings either on coverage changes or through different carriers, or to discontinue providing the benefit. This can be performed in

conjunction with other Risk Management analysis performed and recommended increases in contributions and co-payments.

Salaries

1. **Renegotiate Contracts - Consider Layoffs.** The City must give strong consideration to renegotiating all contracts and request a reduction of salary and benefit increases above benchmarked percentages. Layoffs should also be considered as part of this process if necessary. As an example, the SEIU employees received an approximate 9% increase in salaries and wages from the prior year which is not in line with the wage and raise freezing and other cost avoidance measures being employed in cities across the country. A drop to a wage increase of 3% would equate to a savings of approximately $1,000,000.
2. **Overtime.** The City should scrutinize and cut back on all non-essential overtime. Management directives should be given to ensure the implementation of a stringent policy going forward.

Cost/Benefit/Rightsizing Analysis

1. **Employee Early Retirement - Shared Service Center.** The City has a large number of employees nearing retirement age. The City should investigate the feasibility of an early retirement incentive option for employees nearing retirement which could be coordinated with an analysis to determine the feasibility of moving back office functions to a shared service center approach along with position succession planning.
2. Consider comprehensive review of back office services in a shared service center approach versus performing internally to gain economies of scale and eliminate benefits risk. Areas for consideration should include at a minimum:
   - Payroll
   - Purchasing
   - Accounting and Finance
   - Human Resources
   - Parks and Maintenance
   - Facilities Maintenance

Benchmarking

1. The City should perform benchmarking of private industry as well as similar governments and not for profits to determine ideal headcount and organizational structure, benefits, scope of services, efficiency ratings, best management practices, etc.
2. The City should also conduct comprehensive benchmarking related to best in class comparable cities and companies financial practices to ensure a sustainable finance model.
3. The City should ensure that the organization is accountable (tied to performance) to these best in class benchmarking results.

4. The City should continue to be proactive with competing out all externally purchased insurance and should also consider any insurance savings as a result of a proactive safety program.
5. The City should perform an analysis of the cost/benefit/risk of being self-insured versus obtaining insurance for all risk areas.
6. The City should review its schedules for permits, false alarms, police reports, use of City property, and other such services to determine if they are representative of the City's life-cycle costs including all administrative and overhead expenses. A comparison of these schedules should be performed with other neighboring municipalities and the City should maximize fee for service opportunities and have dynamic fee structures that incorporate full rollup of costs.
7. The City should perform a comprehensive fleet analysis including lease versus buy and bidding procedures for purchase of vehicles, etc.
8. The City should perform a detailed analysis of consulting and professional services and determine evolution over the past 5 years and potentially mandate across the board cuts in these and other escalating categories.

Best Practices

1. Employ zero-based, pay-as-you-can-afford budgeting measures to ensure that expenses never outpace revenue received and that the organization is living within its current year operating budget without relying on fund balance to sustain the organization. This may mean that levels of service may be cut back or vital expenditures be foregone until they can be afforded within the current operating budget.

A structural budget modeling change should be made which ensures that a balanced budget approach is defined as having the current year operating revenues equal expenses. Each month, detailed forecasts should be used to ensure that unfavorable trends are analyzed and management reacts promptly with expense reductions to match revenue shortfalls.

2. As noted above, the City should strive to institute immediate expense reductions equal to the shortfall in revenue to ensure a balanced budget approach.
3. All City departments' should consider scrutinizing headcount evolution for the past 5 years and make adjustments to escalating areas.
4. The City should consider the imposition of a hiring freeze, which includes all openings from resignations/terminations/retirements.
5. The City should perform detailed analysis of all significant expense categories and accounts to determine ideal level and ensure management is maintaining at minimal levels based on mandated cutbacks. This should include focus on consulting and professional services and could potentially lead to fee for service giveback or other reductions.
6. The City should perform an analysis of the potential cost savings in re-issuance of all City bonds and loans but be sure that any cost savings go directly to paying down the existing debt level.

7. Regionalized activities should be analyzed to determine if participation will result in net financial gain. The City should consider the benefits of regional approaches to Sewer and Water that maximizes leverage of their assets while minimizing risk and other cost avoidance strategies.
8. The City should institute a comprehensive Working Capital Management program. The City should aggressively pursue best management practices as it relates to Working Capital Management, including fast collection of receivables (or discounting/factoring of receivables), prompt deposit of monies received, maximizing the return on the cash in the bank while minimizing the fees, management of inventory to as needed basis and best levels of fixed assets (shared assets versus assets with high idle time), aggressive purchasing negotiation to extend terms, reduce cost per unit, and implement pooled purchasing power throughout the region with partners, and consider P cards, EBD purchasing, etc. for small dollar items.

   As an example, based on the City's 2008 level of spending of $98MD, an increase in 1 day's payment terms (paying by contract one day later on all purchases) would result in a cash flow savings of approximately $300KD. The City has tremendous purchasing power and could utilize that power to increase their payment terms substantially, potentially saving millions in cash flow.

   The City should consider best cash flow practices in funding benefits such as employee co-pay on more frequent basis to leverage dollars in bank to use for payments. There are also possibilities to maximize pooled purchasing and leverage purchasing dollars and price decreases. The City should pursue more aggressive recovery of sewer and water bills owed and consider the benefit of hiring collection agency as done for other receivables.

   Another example, as it relates to pooled purchasing, is the use of comprehensive and systematic pooled purchasing methods. The Lehigh Valley Association of Colleges (LVAIC) and the Association of Independent Colleges and Universities in Pennsylvania (AICUP) are examples of purchasing consortiums used for shared service purchases that have saved significant dollars each year. This same method could be employed with surrounding cities, counties, and municipalities.
9. The City should aggressively pursue getting businesses on the tax roll by utilizing information technology to allow parking enforcement personnel to spot businesses and cross check their business information to determine if all Business Privilege Taxes, Earned Income Taxes and License Fees have been paid, or if not, enforcement action is taken to recover all required revenues.
10. The City should perform an organizational review to determine ideal level of staffing, tasks, efficiencies, and services provided with a focus on robust tools for analysis. This should be considered to ensure ideal level of service and matching staff. Analysis components are critical to dynamically managing the budget and day to day operations. Indications are that there is a risk in this area with lack of data analysis and opportunity to perform analysis that can focus on areas for additional improvement. This point cannot be overemphasized as dynamic management

ensures that opportunities are identified and capitalized on in a timely manner which affects cash flow and financing of the City's operations.

11. The City should conduct a Facility Consolidation and Optimization review to ensure efficient use of facilities and corresponding costs and perhaps consolidation of facilities.

    As an example, if an analysis determines that there needs to be 1 fewer fire stations required for the same level of service, this reduction, assuming 30 firepersons, could result in an approximate annual reduction of $3MD.

Development of New-tax parcels/cost avoidance

1. The City should perform a cost/benefit analysis of the potential sale of any/all City-owned or influenced properties, including the municipal golf course. The City should sell all properties that are not essential to City operations, and achieve both the one-time sale proceeds as well as the on-going tax revenue from private ownership. Proceeds should be used to pay down the outstanding debt or fund the pension liability.
2. The City should perform a cost/benefit analysis of the potential sale of any/all Authorities and determine possibility of reorganizing, sale, or dissolution. Proceeds should be used to pay down the outstanding debt or fund the pension liability. The City should also consider performing a study of the Allentown Housing Authority to determine if its cost beneficial to retire the authority and consider either selling all the properties to private investors and add to the tax base, or create a municipal REIT alternative from all holdings (properties can have restricted use covenants placed in the deeds that protect the markets for elderly, low income, half-way houses, middle income rental, commercial, etc). Consider cost benefit/savings of hiring a REIT professional manager. Taxpayers would be able to buy preferred shares, common shares available to the general public.
3. The City should consider requesting that all parties that receive a contribution of personnel, services, or assets and their maintenance from the city, share or assume the cost of those services in the future. As an example, the City of Allentown provides the Allentown School District with School Resource Officers, School Crossing Guards, and fixed assets purchases such as cameras and equipment, along with the ongoing costs of operation and maintenance. The City of Allentown presently provides for the full cost of these items without contribution or reimbursement from the school district.
4. The City should review all of the other funds, including the enterprise funds, to determine if trend is sustainable or whether fees should be raised.
5. The City should perform sale/leaseback analysis for all significant impact areas.

Other

1. The City should ensure that all management comments included in the external audit letter are implemented promptly.

City of Allentown Blue Ribbon Panel on City Finances
Revenue Sub-Committee

- An analysis of each revenue line item for the purpose of evaluating the efficiency of each should be pursued. Criteria to be researched should include:

  - ❖ Is each source of revenue being fairly and aggressively pursued;
  - ❖ How does each compare with other municipalities; and
  - ❖ What is the cost of implementation? This is a combination of evaluating each for its efficiency and its cost-benefit to the City

- A program of Payment In Lieu of Taxes (PILOT) for those entities in the City that, because of their non-profit status, are not required to pay the taxes that for-profit entities are subject to. It is suggested that the City seek out the experiences of other municipalities in the implementation of similar programs. Organizations such as the Pennsylvania League of Cities & Municipalities, the National League of Cities, the US Conference of Mayors and the Government Finance Officers Association would be excellent resources for this research. One very key question here is: what are other cities getting for their PILOT programs and what are they giving up to get this?

- The Sub-Committee recognizes and supports the already existing efforts that the City has been diligently exploring in the innovative areas of Asset Related Potential Revenue and Marketing Based Revenue Opportunities (MBRO). While these efforts may not produce immediate ('09) new revenues, many offer a permanent and positive impact on the revenue side of the City's ledger. Such concepts include but are not limited to:

  - ❖ The sale of certain city owned property;
  - ❖ The development of certain non-city owned but yet still tax-exempt property; and
  - ❖ The pursuit of certain market-based revenue opportunities (MBRO).

- There are other longer-term ideas that the Sub-Committee examined and encourages the further exploration of. These include:

    - ❖ Leasing out of certain available land as a Solar Farm;
    - ❖ The bottling and selling of Allentown water – in order to realize higher margins; and
    - ❖ The possible sale of additional City-owned lands that are of high market value to for the purpose of private commercial development, thus putting potentially high value ratable parcels back on the City's tax rolls.

Minutes from the Investment Committee

Attending were Paul Marin, Chair, Sandra O'Neill, Joel Gilley, Ibolya Balog.

The meeting was called to order by Paul Marin at 4:05 pm.

The meeting started with a review and discussion of ideas suggested at the Committee's prior meeting with a focus on the underfunded pension liabilities. The idea to use hard assets, including real estate, to satisfy the liability was explored, and needs further research as to detailed structure on how it could be implemented and what the effects on rights, obligations and credit agreements would be.

Act 205 – Senator Pat Brown's office informed Paul Marin that it is not likely to see the changes that would be helpful to the City of Allentown before state budget is resolved and adopted in Harrisburg. The state budget is required to be adopted by June 30th, but it is likely to take longer this year due to the deficit. As such, it is not in the time frame for what this committee needs to report back by the June 22, 2009 meeting of the Blue Ribbon Committee.

Next a discussion on the need to consider reopening and renegotiation of contracts with the City labor unions was held. Due to the extraordinary economic circumstances this is a necessity for all entities both in the private and public sectors.

With respect to the various Pension Boards, the need to receive monthly flash reports by board members about investment performance and balances was suggested, so more timely actions can be considered.

The Committee developed the following short and long term options to recommend:

Short Term – in the current year:

1. Consider renegotiation of City union contracts – including pension aspects
2. Consider the use of hard assets for satisfying unfunded pension liabilities
3. More in depth risk assessment of investments including the consideration of the structure of investments.

Long Term:

1. Changes in Act 205 – work with state legislators to enact changes in Act 205 to solve long term pension obligation issues.
2. Appoint an investment professional to serve on the Pension Board, subject to meeting conflict of interest restrictions.

With respect to the City of Allentown General Fund the discussion focused on the cash management. It was noted that the current cash management was a more passive model and benefits may be obtained by focusing on a more active mode, including consideration of interest spreads and optimization of cash flows.

The meeting concluded at 5 pm.