
Fixing Pittsburgh's Finances to Avoid Bankruptcy:

A Problem in Institutional Design

or

Confessions of A Fiscal Social Worker

Robert P. Strauss¹

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The Martin School
of Public Policy & Administration
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¹ Professor of Economics and Public Policy, Carnegie-Mellon University, Hamburg Hall, Pittsburgh, Pennsylvania, 15213-3890. Email: rs9f@Andrew.CMU.Edu; Home Page: www.heinz.cmu.edu/~rs9f.

1. Introduction

Objective of seminar is to

Review the lessons learned from dealing with NYC's financial problems in the 1970's

Determine if and how they may be applied to Pittsburgh's financial situation.

Both bailouts are examples of institutional design problems.

They indicate how important it is to get incentives properly organized in highly charged political environments.

Note:

The Pittsburgh situation is a “work in progress.”

Whether or not the sort of commitment mechanism that has been suggested will work remains to be seen.

Remarks Organized as Follows:

- **NYC and Lessons Learn**
- **Pittsburgh's Travails**
- **A Home Town Solution**
- **Effecting Change: NYC vs. Pittsburgh**

2.0 New York City's Crisis and the Congressional Tax Committees

Two federal tax issues arose:

--- interest on federally guaranteed NYC debt taxable or not?

--- NYC pension plans allowed to hold large fraction of portfolio in City paper?

Background:

Upon joining JCT in July, 1975, assigned to the NYC financial problem;

Bond market closed to NYC, NYC had a "moratorium on debt service"; Felix Rohatyn structured an agreement that allowed the City to stop making pension contributions for a while, and required the plans to buy City paper.

The SEC investigated whether or not NYC intentionally misled investors about the real risk of default. NYC had state exemption from GAAP, and was found to be essentially "not auditable."

General Hysteria in NY, DC

Some policy outcomes:

- **The guaranteed debt was made taxable under the IRC which was a huge turn in constitutional history;**
- **The plans were allowed to buy the paper, but the conditions were a complex balancing act for Bill Simon**

Mechanism for Solvency --- Public Disclosure

GAFR, GAAP, Real Accounting System

\$25 million to Arthur Andersen

A few memorable personal experiences:

Ways and Means Committee blamed me for Banking Committee's violation of their jurisdiction;

Deputy Treasury Secretary Carswell asked Ways and Mean Chair Ullman to fire me; he refused. Committee then had NYC bills switched on them. Complex parliamentary situation.

Congressman Rangel threatened to throw me out of his office window (first floor) when I suggested in a big meeting to look at bankruptcy as an option.

3.0 Pittsburgh's Financial and Political Problems

Bankruptcy an Old Pittsburgh Economic Development Strategy

1878 Default on \$5 million (\$81,177,266 today) sewer bonds for annexation

Pittsburgh's Urban Problems:

Tax Exempt Property in City

Net Exodus of Middle Class Taxpayers

Huge Population Decline

Inelastic Tax Base[s]

Increasingly Dependent/Elderly Population

State Imposed Final Offer Binding Arbitration

No Taxation of Non-Resident Workers

High Ratio of Non-Resident to Resident Workers

Real Estate Assessment Woes

Dysfunctional Board but Fiscally Sound Schools

No State GRS

State Constitutional Constraints

Uniformity Clause

Prohibition on "Special Bills"

Strong Non-interference in Local Affairs

Pittsburgh Home Rule Charter Constraints

**Strong Mayor Form of Government
Elected City Controller Not Independent Auditor
No GAAP or GAFR Requirements**

State Collective Bargaining Constraints

Final offer binding arbitration

Policy Mistakes

**Issuance of non-callable bonds for pension amortization
No Layoff Clauses for Fire, AFSCME employees
Real estate tax relief through homestead exemption
TIFs valued at 10% of Real Estate Tax Base
Economic Development Strategy Failed
No Housing or Parking Strategies of Note
Stadiums instead of Productive Public Works
2003 Budget Imaginatively/Illegally Balanced**

Political Situation

**Mayor Murphy Unpopular in Harrisburg
Mayor Murphy Unpopular among Local Democrats
Current Impeachment Effort before Local Court
Governor's Education Budget Boxed in Harrisburg**

Pittsburgh's Financial Opacity

**Public Authorities
Subsidiary Corporations**

4.0 Fashioning a Home Town Solution

Step 1: Finding Out the Facts

Early Tribune-Review '00 Study: Pittsburgh in Crisis

Spring, 2003 State and Local Finance Course *Practicum*

**Tapping the personal network: City, School District,
Harrisburg**

Newspaper Reporters as Allies

Result: Two Perspectives on the City Debt

First Perspective

Figure 1: PNC Capital Markets Debt Service Chart

Figure 2: Debt Service as % of Operating Expenditures

Second Perspective

Table 1: City, Authority, and Pension Debt

Table 2: Per-capita Debt

Step 2:
Identifying Political Constraints

**Little Confidence in Mayor and Council to Budget
Democrats in Senate and House Won't Help
State Republicans Afraid of interest rate effects**

Step 3:

**Time Consistent Home Town Solution, no Control
Board:**

Goal:

**\$100 million/year budget swing needed to pay debt
service, get back into bond market**

Solution:

**Financial Transparency a Primary Objective:
GAFR, GAAP; consolidation; public records;
Safe Haven from Final Offer Binding Arbitration
Public Approval of Union Contracts**

**Spending Reductions -\$22.5 million
Temporary Tax Increases (2 years)
Wage Tax +\$49 million
Real Estate +\$23 million**

State determination of compliance for 2 years

THEN:

Commuter Taxes of \$12 million/year upon continued compliance per above.

Note: downgrading of Pittsburgh bonds to junk very traumatic; fastest decline in 100 years

Sidebar 1: Mayor's Commission on Pittsburgh City Schools didn't work.

Sidebar 2: Where is the SEC? Would a 10B Investigation matter?

Sidebar 3: Other Strategies

Act 47 State Distressed Municipality Status

Federal Bankruptcy Court

5.0 Effecting Change in NYC and Pittsburgh

Personal Setting:

NYC: Working for JCT

PGH: Citizen

Financial Setting:

**NYC bonds uninsured; commercial banks worried;
NYC influential in Albany, DC; SEC Investigation**

**PGH bonds insured, little influence in Harrisburg, not a
DC issue; Pittsburgh vs. Philadelphia an issue**

PGH Mechanism:

Public Statements

Public Solutions via written documents

Private advice to members of legislature.

A Comment on the “Postponed Public Hearing”

Final Prediction:

General Assembly Bill Vetoed in late November

Serious cash crunch in early 2004

Act 47 notionally triggered

Federal Bankruptcy Court by April, 2004.

Appendix: State Constitutional Constraint Language

Article VII Taxation

Section 1.

All taxes shall be uniform, upon the same class of subjects, within the territorial limits of the authority levying the tax, and shall be levied and collected under general laws.

Article III. Legislation

Delegation of Certain Powers Prohibited

Section 31.

The General Assembly shall not ... interfere with any municipal improvement, money, property or effects, whether held in trust or otherwise, or to levy taxes or perform any municipal function whatever.

Certain Local and Special Laws

Section 32.

The General Assembly shall pass no local or special law in any case which has been or can be provided for by general law and specifically the General assembly shall not pass any local or special law [that has the effect of:]

1. Regulating the affairs of counties, cities, townships,

wards, boroughs, or school districts.

Nor shall the General Assembly indirectly enact any special or local law by the partial repeal of a general law; but laws repealing local or special acts may be passed.

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