City Council
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402 City Hall
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Legislation Text

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TO THE PRESIDENT AND MEMBERS OF THE COUNCIL OF THE CITY OF PHILADELPHIA:

I am returning herewith as disapproved Bill No. 040767, passed by the Council on June 2nd, 2005. This Bill would impose annual reductions in both the gross receipts and net income portions of the Business Privilege tax through 2017, in addition to the wage tax and gross receipts tax rate reductions and low-income wage tax credits already scheduled by law to take effect.

The Administration projects that this Bill would result in the loss of $22 million in revenue currently assumed over the FY06-FY10 Five-Year Plan, and the loss of an additional $570 million over the course of the following five-year period. The total revenue loss to the City from the Bill by the end of its effective date, assuming current revenue growth rates and tax reduction plans, is projected to be over $1 billion. The City can not afford these revenue losses. These would leave the City with fund balances below the levels requested by the Pennsylvania Intergovernmental Cooperation Authority (PICA) to offset the possibility that the Philadelphia Gas Works would not repay $81 million in FY09 and FY10.

The revised Five-Year Plan submitted to Council on May 24th reflects the layoffs imposed this fiscal year and the elimination of over 2,000 budgeted positions in a two-year period. In order to offset funding restorations requested by Council members without further painful position eliminations and service impacts, City Council and the Administration worked together to pass legislation providing *expanded* revenue sources. Enactment of this Bill would promptly undo that effort and leave the City with few options for balancing the Plan, short of workforce reductions beyond what are already historically low levels, at a time when we are attempting to address numerous concerns about the Plan raised by PICA and mentioned in my May 24th letter.

Finally, let me remind you that the Plan does not include any wage increases for our workers after FY08, which would be even more difficult to fund after the revenue losses imposed by this Bill. More critically, the current FY 06 Budget or the FY 06 to 10 Five Year Financial Plan make no provision for addressing the potential state cuts that over the years have provided support for critical social service prevention programs. Under the

Govenor's current state budget proposal, the City will be forced to eliminate at least $50 million in spending on programs to prevent child abuse and youth violence, if the City is unable to provide matching funds of approximately $10.5 million. If Commonwealth, in fact, changes its funding formulas and the City does not identify $10.5 million in matching funds, 23,000 youth will not be able to participate in after school and truancy and delinquency prevention programs, more than 6,300 children and families will lose access to parenting programs, intensive home visiting for young at-risk parents, and school based services.

Beyond the immediate need to balance our Plan, I do not support "back loading" tax reductions after the statutory five-year financial planning period mandated by the PICA Act. The tax rate reductions in Bill No. 040767 would accelerate sharply beginning in FY11, just as the wage tax rate reductions enacted last year in Bill No. 040607 accelerate sharply beginning in FY10. The low-income wage tax credits enacted in Bill No. 040397 were back-loaded to FY 10 and beyond and, therefore, not reflected in after last year's Plan. If Bill No. 040767 becomes law, the combined impact of all these delayed reductions is likely to cause tax revenues to fall in each year, as shown in Attachment A to this letter. How can we ask the future leaders of Philadelphia to accommodate far higher levels of tax reduction than we find we are able to handle now?

The City's ten-year program of incremental wage and business privilege tax reductions, while meaningful, has generally been moderate enough to be offset by economic growth and efficiency measures, although the effect of tax reductions during the down economy eliminated any wage tax growth in FY03 and increased the size of business privilege tax losses in FY02 and FY03. However, the size and effect of the tax reductions and credits already scheduled will increase dramatically beginning in FY10, to the point that it would be difficult for economic growth to offset the effect of the tax reductions. Bill No. 040767 would pile onto this effect and guarantee that tax revenue growth would have to be over twice as large as projected inflation levels in order for the City to avoid collecting less and less tax revenue in each year. No one has disputed this calculation.

The Five-Year Financial Plan document, and numerous other communications from my Administration have also made clear that economists indicate that even a speculative "supply-side" economic effect would only offset 15 to 20 percent of the City's revenue losses from tax reductions over a Plan period, an effect that is already reflected in our Plan by optimistic revenue assumptions that Fitch Ratings characterized as "overly reliant on economic development." While I support manageable tax reductions and reform in order to improve our local economy, additional tax reductions would not pay for themselves, and would further weaken our finances or force service reductions that, the economists tell us, would undermine the very value of the tax reductions. The data indicates that pursuing unmanageable tax reductions in a vacuum as a strategy to improve the City's finances is about as sensible as it would be for General Motors to sell cars for $2,000 that it cost them $10,000 to build.

The City must increase its economic competitiveness by restructuring its tax system. We are cutting our wage tax rates, every year. We are cutting our gross receipts tax rates, every year. We are scheduled to implement low-income wage tax credits in FY10. We expect that we will provide even more wage tax relief through gaming by 2007 or 2008. Over the past several years we have enacted more and more tax reductions, even as the City's fund balance dwindled to the first negative fund balance in twelve years. No other city in the country is doing anything like this! Some of our peers have raised taxes. Some of our peers that were cutting taxes paused due to the bad economy, while here we not only kept going in the face of deficits, we passed even bigger tax reductions. The Tax Reform Commission's report stated that in the long run real estate taxes in Philadelphia should be higher to offset revenue losses from tax reductions. We should be open and honest about that. We should be explicit about the tradeoffs that are necessary to balance a budget, any budget, whether it is for a household, a business, or a government, and package any additional tax reductions with specific plans for offsetting them with other revenue sources or the elimination of programs. Until then, I can not support legislation like Bill No. 040767.

Respectfully submitted,
John F. Street
Mayor

Attachment