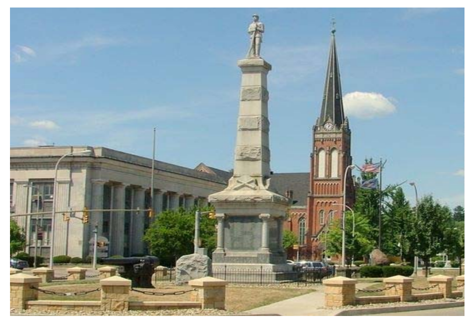
Municipalities Financial Recovery Act

Financial Condition Report

City of New Castle
Lawrence County, Pennsylvania





Prepared on behalf of the

Commonwealth of Pennsylvania
Department of Community and Economic Development
Governor's Center for Local Government Services

As revised and filed with the City on April 1, 2019

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Table of Contents

Introduction

On October 31, 2014, Governor Tom Corbett signed Act 199 (formerly House Bill 1773) into law, which made several significant changes to Act 47 oversight. In response to concerns that many municipalities that enter Act 47 oversight remain there for years, Act 199 limited the amount of time that a municipality can remain in Act 47 oversight. For communities like New Castle that are already in Act 47 oversight, the relevant provision is the following:

> *"Municipalities operating pursuant to a recovery plan on the effective date of this section shall be subject to a termination date five years from the effective date of the most recent recovery plan or amendment enacted in accordance with this act…"*

As such, New Castle's termination date is December 2019, which is five years from the effective date of the Plan amendment adopted by the City in December 2014. Act 199 requires that, no later than June 30, 2019[1], the Recovery Coordinator – Eckert Seamans Cherin & Mellott, LLC (Eckert Seamans) and Public Financial Management (PFM) – review New Castle's government finances and make a recommendation to the Secretary of the Pennsylvania Department of Community and Economic Development for one of the following actions:

- New Castle's distressed status be terminated and the City exits Act 47 oversight;
- A three-year exit plan be adopted;
- Conditions are such that New Castle should be disincorporated[2]; or
- New Castle be declared in a state of "fiscal emergency" with the possibility of receivership.

This Report reviews the City's financial and operational progress since entering Act 47 in 2007 and recommends that a three-year exit plan be adopted for New Castle.

The Coordinator projects that the City will continue to struggle with maintaining fiscal balance, and the structural challenge – balancing recurring expenditures against recurring revenues – will be heightened in the next three years as the City eliminates the additional taxing authority provided by Act 47. Beyond having to close the deficits created by eliminating the Act 47-authorized tax and an eroding tax base, the City will also have to find alternative funding for capital improvements once the Act 47 EIT is eliminated so that it has the infrastructure to continue providing critical municipal services to its residents and businesses.

While this Report articulates current financial conditions and ongoing challenges that the City must continue to tackle for the next three years as it prepares to exit oversight, the three-year exit plan (which will be released within 90 days of the public meeting on this Report or the filing of a revised version of this Report, whichever is later) will provide strategies designed to provide New Castle a better chance of successfully exiting Commonwealth oversight at the end of 2022.

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[1] The statutory deadline is "not later than 180 days after the beginning of the final year of distressed status," which is 2019.

[2] This action is only applicable for municipalities that do not provide police service or fire service through its employees, according to Chapter 4 of the Municipalities Financial Recovery Act, and is not applicable to New Castle.

Progress under Act 47

New Castle's population has been declining for decades and the weakness in its economy precedes the City's designation as a financially distressed municipality. New Castle has long had higher poverty rates, lower median household incomes, and lower median home values than the nation, the rest of Pennsylvania, and the rest of Lawrence County (the County).

The gap between New Castle and these comparison points has grown over time. In 2000, New Castle's poverty rate was 71.9 percent higher than the County as a whole and 89.0 percent higher than all of Pennsylvania. The most recent census data shows New Castle's poverty rate is now 94.3 percent higher than the County's and more than twice Pennsylvania's rate.

	2000 Census	2013 ACS	2017 ACS
% of individuals below poverty level			
New Castle	20.8%	25.8%	27.2%
Lawrence County	12.1%	14.4%	14.0%
Pennsylvania	11.0%	13.3%	13.1%
United States	12.4%	15.4%	14.6%
Median household income			
New Castle	$25,598	$29,559	$31,044
Lawrence County	$33,152	$43,546	$47,188
Pennsylvania	$40,106	$52,548	$56,951
United States	$41,994	$53,046	$57,652
Median home value			
New Castle	$42,300	$57,800	$62,000
Lawrence County	$72,200	$96,700	$102,300
Pennsylvania	$97,000	$164,700	$170,500
United States	$119,600	$176,700	$193,500

In addition to these economic weaknesses, the City had a very poor financial record before it entered Commonwealth oversight. Before a single employee reported for duty in 2007, the City already faced a multi-million dollar deficit. The City was behind on its annual obligations to the employee pension plans and accumulated $4.0 million in debt related to its misuse of Tax Revenue Anticipation Notes (TRAN).

Other large liabilities also existed. The City had a long-running lawsuit involving eminent domain actions taken by the Redevelopment Authority in the 1970s and a swap agreement that generated another multi-million dollar liability. On top of those liabilities, the City was in danger of running out of cash in late 2007, putting its ability to make payroll and pay its vendors at risk.

Entering Act 47 Oversight

In January 2007, the Secretary of the Pennsylvania Department of Community and Economic Development (DCED) designated New Castle as distressed according to four of the eleven criteria in Act 47. The Department appointed Eckert Seamans and PFM as the City's Recovery Coordinator and the firms worked with the City's elected and appointed officials on the original Recovery Plan.

The 2007 Recovery Plan contained several measures to place the City's finances back into balance – increases in the real estate tax, resident earned income tax and commuter earned income tax; higher fees for some services like trash collection; wage freezes; fewer paid holidays; and new health insurance cost sharing arrangements for City employees.

In late 2007, the Commonwealth gave the City a $750,000 interest-free loan to help meet its cash flow needs for the rest of the year. The City also needed an unfunded debt borrowing to repay the prior year's pension obligation and the $4 million in TRAN debt. An unfunded debt borrowing is a rare transaction where the City has to secure court approval to issue debt, often at a higher interest rate, to retire prior year's obligations or cover current year operating expenses.

With those measures in place, the City ended its streak of annual operating deficits in 2009. It retired its prior year's obligation to the employee pension plans and started making its annual contributions on time every year going forward. Helped by an asset sale in 2010, the City repaid the unfunded debt borrowings several years ahead of schedule. The City has also resolved the swap claim and settled the long-running eminent domain law suit.

Just as important, the City has improved its financial management. With the support of DCED and the Recovery Coordinator, the City upgraded its financial management software and improved its budgeting, procurement, and accounting practices. It started generating periodic financial reports that give City Council and the public a clearer sense of City's financial performance and condition.

2012 Amended Recovery Plan

In 2012, the Coordinator wrote a comprehensive amendment to the Recovery Plan in response to the City's ongoing financial challenges and an emerging threat that many local governments face – rapidly rising required contributions to the employee pension plans. For reasons described in the 2012 Amended Recovery Plan, the funded ratio for those plans slipped from above 80 percent as of January 2007 to 55 percent as of January 2013. Consequently, the City's annual contributions to the plans were projected to jump from $1.3 million in 2007 to $3.0 million in 2015 at the time the Coordinator wrote the 2012 Amended Recovery Plan.

The 2012 Amended Recovery Plan put a strategy in place for incrementally increasing the City's annual pension contributions to improve the funding levels; avoiding costly benefit enhancements for current or past employees; and establishing a more affordable level of benefits for new hires. As of January 1, 2017, the aggregate funded ratio across the three pension plans was 65 percent – still too low but better than 55 percent. In recognition of the City's continued progress in its financial management, Standard & Poor's upgraded the City's underlying credit rating in 2014 by two notches from BBB to A- and cited the City's "strong [financial] management despite recent fiscal challenges" in its credit rating review[3].

2015 Amended Recovery Plan

In 2014, Governor Tom Corbett signed Act 199 into law, which sets the deadline for a determination on New Castle's readiness to exit oversight by the end of 2019. One factor for determining New Castle's readiness to exit oversight is whether the City can balance recurring expenditures against recurring revenues without the additional taxing authority provided by Act 47. Because DCED had advised the Coordinators that the 2015 Amended Recovery Plan could not presume that the City would subsequently use the three-year exit plan option, the 2015 Amended Recovery Plan assumed that the Act 47 portion of the earned income tax (EIT) would be completely eliminated by 2019 and set a strategy that allowed the City to retain some of the EIT revenue while still moving the City toward exiting oversight. By shifting part of the Act 47-authorized EIT to an EIT authorized by Act 205 of 1984 (i.e. the distressed pension EIT), the City was able to keep some of the revenues that would otherwise be eliminated.

The 2015 Amended Recovery Plan also placed measures to help City government control its personnel spending, including setting a workforce allocation for its bargaining units and non-represented employees and placing a five-percent cap on growth in the City's share of health insurance costs. Other strategies to close the projected budget deficits included levying a stormwater fee, improving real estate tax collection rates, and recovering costs to pay for the City's trash collection operations.

[3] Standard and Poor's credit rating review, June 2014.

While these initiatives were helpful and necessary, they still did not close the projected deficit. The 2015 Amended Recovery Plan therefore used the one locally-controlled revenue option available to help the City generate enough money to help bridge the gap – a real estate tax increase. The 2015 Amended Recovery Plan anticipated the City would need to increase its real estate tax rate by nine mills (or by 77 percent) over the five-year period from 2015 to 2019. To date, the total real estate tax rate remains lower than projected in the Plan, in part because the City generated additional revenues through improved tax collection and reduced expenditures through attrition.

Real Estate Tax Rates (Mills)

	2015	2016	2017	2018	2019
2015 Plan projection	11.726	12.726	15.726	18.726	20.726
Actual rate	11.726	12.726	13.726	14.226	14.226

But the main reason the City has been able to avoid the large real estate tax increases as described in the 2015 Amended Recovery Plan is because it has not reduced its Act 47 EIT rate at the pace anticipated in the Plan.

In 2018, DCED advised the Coordinators that New Castle can keep its Act 47 EIT as long as the City remains under Act 47 oversight. Thus, if a three-year exit plan is adopted in 2019, the City would be able to keep its additional taxing authority through 2022, the end of the exit plan period.

With new guidance provided by DCED, the Coordinator wrote a Plan Amendment in 2018 that allows the City to keep half of the Act 47 EIT for operational purposes. Pursuant to the 2018 Plan Amendment, the City now levies a 0.4 percent Act 47 EIT on residents and a 0.3 percent Act 47 EIT on commuters and uses half of the Act 47 levy to fund operations and the other half to fund capital projects.

2019 Resident EIT Rate

Act 511 - School District	0.50%
Act 511 - City	0.50%
Act 47 - Operations	0.20%
Act 47 – Capital (Paving)	0.20%
Act 205 - Distressed Pension	0.70%
Total	**2.10%**

2019 Non-Resident (or Commuter) EIT Rate

Act 511 - Home municipality	1.00%
Act 47 – Operations	0.15%
Act 47 – Capital (Paving)	0.15%
Act 205 - Distressed Pension	0.70%
Total	**2.00%**

Readiness to leave oversight

The 2015 Amended Recovery Plan sets forth four primary objectives that the City should achieve to exit Act 47 oversight:

- Eliminate the operating deficits in the Amended Recovery Plan baseline projection without relying on non-recurring resources, such as fund balance, to cover recurring expenditures;
- Keep the City's reserves at an appropriate level;
- Phase out the use of the resident and non-resident EIT authorized by Act 47; and
- Provide more funding to improve the City's existing infrastructure (e.g. road repaving, building renovations).

These are not the only objectives that the City should meet to exit Act 47 oversight, but they provide a useful measure of the City's overall progress toward existing oversight. Eliminating operating deficits in the baseline projection is also one of four factors the Secretary of DCED will consider in determining whether the conditions that led to a determination of municipal financial distress are no longer present.

The following summarizes the City's progress in achieving these four objectives since adopting the 2015 Amended Recovery Plan.

Eliminate projected deficits

The City finished 2015 with a small deficit and had operating surpluses in both 2016 and 2017 across the General, Sinking, and Pension Funds. These positive results were achieved primarily through annual real estate tax increases and headcount reductions, as shown in the table below. The surplus in 2017 was also in part because the City underspent its capital budget by $250,000.

Net Operating Result across the General, Sinking, and Pension Funds

	2015 actuals	2016 actuals	2017 actuals[4]
Revenues	20,147,427	18,822,974	19,280,378
Expenditures	20,250,003	18,596,195	18,853,879
Surplus/(Deficit)	**($102,576)**	**$226,778**	**$426,498**

Real Estate Tax Rate	**11.726 mills**	**12.726 mills**	**13.726 mills**
Full-time Headcount	**110**	**112**	**107**

According to Act 47, one of the factors that the Secretary of DCED considers to determine whether New Castle's distress status should be terminated is the City's ability to have positive operating balances. The Secretary will not only consider whether the City has deficits in the years prior to existing oversight, but the City also has to show that it is projected to have positive operating balances for the five years immediately after the termination of distressed status[5].

To determine whether the City is ready to exit oversight, the Coordinator developed a five-year projection showing the City's revenues and expenditures from 2020 through 2024.

Absent corrective actions, the Coordinator projects that the City will have deficits increasing from $1.1 million in 2020 to $3.2 million in 2024 and run out of the fund balance by the end of 2022. While the major driver of the projected deficits is the elimination of the additional taxing authority provided by Act 47, the City also has a challenge in that recurring expenditure growth outpaces recurring revenue growth. The City's real estate tax base has been shrinking, so the baseline forecast projects the decline to continue in the next five years. The next chapter details the key assumptions underlying the five-year baseline projections.

[4] The operating results shown in this table are different from the audit results because the revenues and expenditures in this table does not include approximately $400,000 in spending from the rainy day fund in 2017. The audit also includes several grant accounts which are not included in the actual operating results shown in this table.

[5] Section 255.1 of Act 47.

Five-year Baseline Projection, 2019 -2024

	2019 budget	2020 proj.	2021 proj.	2022 proj.	2023 proj.	2024 proj.
Revenues	19,543,254	19,517,766	19,683,715	19,843,544	18,402,577	17,656,805
Expenditures	19,611,533	20,575,288	21,435,137	22,233,288	21,260,793	20,901,653
Surplus/(Deficit)	**($68,278)**[6]	**($1,057,522)**	**($1,751,422)**	**($2,389,744)**	**($2,858,216)**	**($3,244,848)**
Fund Balance[7]	**$4,803,791**	**$3,746,269**	**$1,994,846**	**($394,898)**	**($3,253,114)**	**($6,497,962)**

Maintain financial reserves

One of the reasons the City's credit rating was upgraded from BBB to A- in 2014 was because it had a strong fund balance level. S&P cited the City's "very strong liquidity position, providing sufficient cash to cover potential contingent liabilities."

As mentioned in the 2015 Amended Recovery Plan, one of the City's successes since entering Act 47 oversight has been its ability to establish and maintain General Fund reserves. The reserves provide a buffer against unexpected revenue shortfalls or unbudgeted expenditures.

Since adopting the 2015 Amended Recovery Plan, the City has incrementally replenished its Rainy Day reserve (officially called Act 47/Mayor/Council Reserves). As of the end of 2017, the City had a Rainy Day reserve of $2.6 million, fulfilling the 2015 Plan requirement.[8] In addition to the Rainy Day reserve, the City also had $5.0 million in unassigned fund balance, equivalent to 25.7 percent of the City's operating revenues.

City of New Castle Rainy Day Reserve and Unassigned Fund Balance

	2017 Audit	2017 Reserves as a % of Revenues
Rainy Day Reserve	$2,559,493	13.1%
Unassigned Fund Balance	$5,028,354	25.7%

One of the reasons the Coordinator recommended the City replenish and maintain its rainy day reserves is because of New Castle's history of financial distress and its lack of capital funding. In both 2015 and 2017, the City used money from the Rainy Day fund for emergency purposes primarily because of its limited capital budget. Moving forward, and as described later in this Report, New Castle's need to maintain adequate reserves will even be stronger as it seeks to exit Act 47 oversight at the end of 2022.

Phase out Act 47 EIT

The 2019 budget follows the 2018 Amended Recovery Plan requirements and shifts half of the Act 47 levy from the General Fund to a fund reserved for capital projects. Based on 2019 budget projections, the City will be relying on $985,000 in Act 47 EIT to fund operations and another $818,000 in Act 47 EIT to fund capital projects. While the City has made progress to phase out of the Act 47 EIT, much more needs to be done in order to completely eliminate the reliance on this taxing authority to deliver basic municipal services.

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[6] The City's 2019 budget shows a $125,000 negative difference between revenues and expenditures in the Pension Fund, but part of that was offset by the use of cash balance in the Sinking Fund, resulting in a total net operating result of $68,278 across the General, Sinking, and Pension Funds.

[7] The $4.8 million is based on the $5.0 million unassigned fund balance as stated in the 2017 financial audit, which does not include the Rainy Day fund.

[8] See initiative AD01 on p. 16 of the 2015 Amended Recovery Plan

If the City replaced the $985,000 in operating revenues funded by the Act 47 EIT solely by increasing the real estate tax, the City would have to increase its tax rate by 2.5 mills, a 17.6 percent increase to its current tax rate (14.226 mills) and 42.6 percent increase to its tax rate in 2015 (11.726 mills). While repeatedly increasing the City's real estate tax rate may mathematically solve the City's financial challenge, it places an even larger burden on residents and business owners and makes advancing economic development initiatives even more difficult given the existing weakness of the tax base.

Act 47 EIT revenues, 2016 – 2019 (on a cash basis)

	2016 actual	2017 actual	2018 actual	2019 budget
Act 47 EIT (Operations)	3,057,898	1,996,234	1,311,611	984,968
Act 47 EIT (Capital)	0	378,102	589,796	817,745
Total Act 47 EIT	**$3,057,898**	**$2,374,337**	**$1,901,406**	**$1,802,712**

Fund capital improvements

Pursuant to the recommendation in the 2015 Amended Recovery Plan[9], the Sanitation Authority started levying a stormwater fee in 2018. The stormwater fee is estimated to provide $825,000 in annual revenues to maintain the stormwater system and for any emergency repairs required as a result of flooding incidents, such as the ones in 2015 and 2017 that caused extensive damage. As a result of the stormwater fee, the City shifted over $100,000 in annual General Fund expenditures to the Sanitation Authority, not to mention the practical benefits of having a funding source that is solely dedicated to the maintenance and upkeep of the stormwater system.

While the City has made progress in funding the necessary capital needs required for its stormwater system, its investments in other infrastructure have declined over the last five years. From 2015 to 2018, the City's capital budget declined from $1.7 million to just above $500,000 in 2018. While the level of capital spending in recent years is consistent with the 2015 Amended Recovery Plan projections, the Coordinator also acknowledged that this is not the ideal level of capital project funding for New Castle. The following table shows how the City has spent its capital budget over the last five years.

2015 – 2019 Capital Budget Allocation[10]

	2015	2016	2017	2018	2019
Vehicles/Equipment	1,084,300	190,500	60,000	250,000	345,142
Infrastructure	280,000	300,000	413,164	200,000	215,103
Building upgrades	25,000	255,000	39,000	20,000	50,500
Recreation Assets	114,200	24,500	90,280	15,000	45,000
Information Technology	10,000	93,800	0	0	0
Other	168,927	138,927	109,927	43,703	162,000
Total	**$1,682,427**	**$1,002,727**	**$712,371**	**$528,703**	**$817,745**

Looking forward, the Act 47 capital EIT will provide a temporary capital funding source for the next three years, but the City will have to find alternative funding for capital improvements once the Act 47 EIT is eliminated beginning in 2023.

[9] See CP02 on p. 40 of the 2015 Amended Recovery Plan.

[10] Grant funded projects, such as the police station renovation, are not included in this table.

The other challenge in maintaining its capital assets is the City's lack of capacity to execute projects. Even though the City has very limited capital funding, the City spent less than budgeted in each of the years from 2013 to 2017. For example, in 2017, the City budgeted $250,000 for road paving but the project was not executed until the summer of 2018. In aggregate, the City underspent its capital budgets by almost $500,000 in the last five years.

Capital Budget and Spending, 2013 - 2017

	2013	2014	2015	2016	2017	5-Year total
Capital budget	375,000	540,000	1,682,427	1,002,727	712,371	**4,312,525**
Capital spending	371,253	408,417	1,619,151	954,854	461,269	**3,814,943**
Overspent/(Underspent)	**($3,747)**	**($131,583)**	**($63,276)**	**($47,873)**	**($251,102)**	**($497,582)**

Readiness to exit oversight

The City has made significant progress since 2007. At a basic level, the City has gone from having at least three consecutive years of annual deficits[11] to being able to balance its budget on an annual basis for the last decade. It has controlled its salary spending by providing moderate wage increases and reducing headcount. On the benefits side, employees have changed to high deductible health plans to control employee contribution growth while allowing the City to remain within the maximum City contributions as governed by the 2012 and 2015 Amended Recovery Plans. The City also established a defined contribution pension plan for its non-uniformed employees hired after 2017 as part of the contract re-openers for pension changes[12].

On the revenue side, the City increased its current year real estate tax collection rate by contracting delinquent tax collections to a third-party collector in 2016, and diversified its revenue streams through the levying of a stormwater fee in 2018. Even though increasing real estate taxes can be a difficult decision because it results in larger burden for home and business owners and makes it even harder for New Castle to attract and retain its residents and businesses, the City increased its real estate tax rate three times in the last four years. This year, the City adopted its budget levying a 14.226-mill real estate tax; 21.3 percent higher than the tax rate when the City adopted the 2015 Amended Recovery Plan.

Nonetheless, there is much more to be done for New Castle to achieve true, long-term financial recovery. Even though the City has been marginally balancing its budget in the last three years, the Coordinator projects that the City will continue to struggle with maintaining fiscal balance, and the structural challenge – balancing recurring expenditures against recurring revenues – will be heightened in the coming years as the City eliminates the additional taxing authority provided by Act 47. The five-year baseline forecast detailed in the next chapter projects deficits growing from $1.1 million in 2020 to $3.2 million in 2024 absent correction, even without any additional capital improvement funding beyond 2022 once the Act 47 EIT is eliminated.

While one of the City's biggest challenges is its demographic weaknesses that is largely beyond the City's control, New Castle can still make progress toward financial recovery by controlling cost growth, increasing cost recovery, and advancing its economic development efforts.

Based on results from the five-year baseline forecast and the evaluation of the four objectives as set forth in the 2015 Amended Recovery Plan, the Coordinator recommends that the City adopt a three-year exit plan.

[11] This is one of the four criteria in Act 47 that New Castle met for being designated financially distressed.

[12] See initiative WF10 o p. 82 of the 2015 Amended Recovery Plan.

Five-Year Baseline Projections

As discussed previously, Act 199 of 2014 made several changes to Act 47 and provided four factors that the Secretary of DCED must consider in determining whether the conditions that led to a determination of municipal financial distress are no longer present. The factors are:

1. Operational deficits have been eliminated and the financial condition of the City demonstrates a reasonable probability of future balanced budgets;

2. Obligations issued to finance the City's debt have been retired, reduced or reissued;

3. All claims or judgments that would have placed the City in imminent jeopardy of financial default have been negotiated and resolved; and

4. The City is projected to have positive operating balances for the first five years after the termination of distressed status.

Before entering Act 47 oversight, the City funded its annual operating deficits using proceeds of Tax Revenue Anticipation Notes (TRANs), effectively pushing deficits forward each year in lieu of balancing the budget. With measures in place to bring the City's finances back into balance since entering oversight, the City improved its cash flow position and reduced the amount of TRANs it needed to maintain its cash flow from $4.0 million in 2007 to $1.0 million in 2013. Since 2014, the City has not issued TRANs to cover cash flow shortages and currently has no other cash borrowings or loans that are required to be repaid in order to exit Act 47 oversight. The City also resolved the litigation over property condemned by the former Redevelopment Authority (McGaffic case) in 2015 and has not had any significant claims or judgments since then. Thus, New Castle fulfills two of the four factors (factor #2 and #3) that it must satisfy in order to exit oversight.

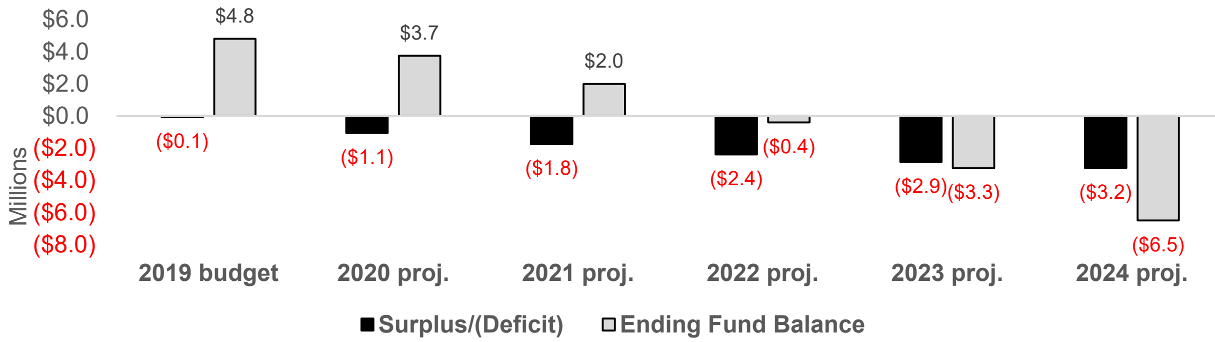
To determine whether New Castle demonstrates a reasonable probability of future balanced budgets (factor #1) and is projected to have positive operating balances in the next five years (factor #4), the Coordinator projected the City's revenues and expenditures in a baseline scenario for five years from 2020 to 2024.

Similar to the Recovery Plan process, the baseline projection uses the most recent adopted budget as the starting point, accounts for known future changes (such as wage increases in existing collective bargaining agreements and scheduled debt payments) and then applies growth rates calculated using a combination of historical performance, socioeconomic trends, and other factors.

For many of the City's revenues and expenditures, the baseline uses the amounts in the most recently adopted 2019 budget and applies growth rates to project future results. On the revenue side, the baseline growth rates are calculated based on the Coordinator's analysis of historical revenue performance and trends in the underlying tax base. Since a large part of the City's locally generated revenue comes from the real estate and earned income taxes, the Coordinator paid particular attention to changes in the total assessed value of taxable real estate and resident and commuter earnings.

The five-year projection starts with the City's marginally balanced 2019 budget. Beginning in 2020, however, the baseline forecast projects a deficit of $1.1 million that will grow to $3.2 million in 2024, resulting in the City running out of fund balance by the end of 2022.

Five-Year Baseline Projection (Includes the General, Sinking, and Pension Funds), 2019 – 2024



	2019 budget	2020 proj.	2021 proj.	2022 proj.	2023 proj.	2024 proj.
Revenues	19,543,254	19,517,766	19,683,715	19,843,544	18,402,577	17,656,805
Expenditures	19,611,533	20,575,288	21,435,137	22,233,288	21,260,793	20,901,653
Surplus/(Deficit)	**($68,278)**	**($1,057,522)**	**($1,751,422)**	**($2,389,744)**	**($2,858,216)**	**($3,244,848)**
Fund Balance	**$4,803,791**[13]	**$3,746,269**	**$1,994,846**	**($394,898)**	**($3,253,114)**	**($6,497,962)**

The next sections of this Report detail the operating revenue and expenditure assumptions underlying this projection as well as the major budget drivers.

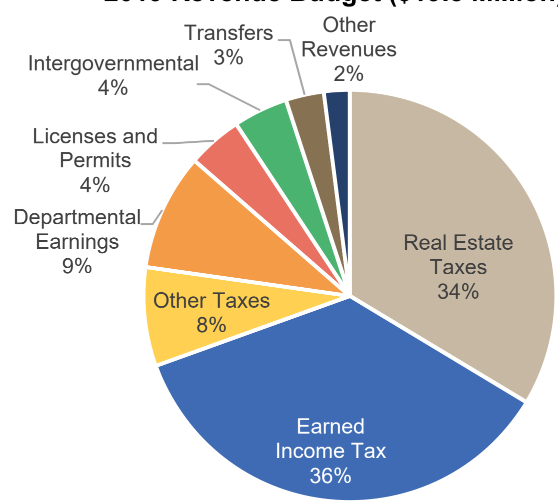
Major Revenue Assumptions

Similar to many Pennsylvania local governments, New Castle's General Fund budget is characterized by substantial income from the real estate and earned income taxes. Seventy (70) percent of its revenues come from these two sources.

In aggregate, the City's operating revenues dropped at an annual compound rate of 0.1 percent from 2013 to 2017, excluding the one-time transfers from the Marcellus Shale gas proceeds for capital projects. Much of this decline was driven by decreases in the earned income and other taxes.

The pie chart to the right shows the major categories of revenues in the adopted 2019 budget, and the table on the next page shows the City's operating revenues, including the General, Sinking, and Pension Funds, from 2013 to 2017.

2019 Revenue Budget ($19.5 Million)



[13] The 2019 ending fund balance is based on the 2017 year-end audited unassigned fund balance ($5.0 million). Both the 2018 and 2019 budgets have small deficits, so the Coordinator applied those projected deficits to the $5.0 million ending fund balance in 2017 and projects $4.8 million in ending fund balance in 2019. At the time when the Coordinator released this Report, the 2018 year-end preliminary actuals was not available.

Revenues across the General, Sinking, and Pension Funds, 2013-2017

	2013 audit	2014 audit	2015 audit	2016 audit	2017 audit	CAGR
Real Estate Taxes	5,973,356	5,704,190	5,955,032	6,491,399	6,366,008	1.6%
Earned Income Tax	7,690,515	7,393,619	7,514,866	6,330,745	7,030,349	-2.2%
Other Taxes	1,472,288	1,432,760	1,283,077	1,380,764	1,303,556	-3.0%
Departmental Earnings	633,829	779,720	587,616	484,602	944,560	10.5%
Licenses and Permits	1,702,969	1,881,314	1,673,489	1,798,732	1,808,298	1.5%
Intergovernmental	811,666	760,092	1,185,430	805,071	841,872	0.9%
Transfer for capital projects	0	408,417	1,209,455	954,854	236,019	N/A
Other transfers	431,730	481,717	392,686	233,312	373,136	-3.6%
Other Revenues	405,493	339,792	345,777	343,494	376,579	-1.8%
Total Revenues	**$19,121,845**	**$19,181,621**	**$20,147,427**	**$18,822,974**	**$19,280,378**	**0.2%**
Revenues excl. capital	**$19,121,845**	**$18,773,204**	**$18,937,972**	**$17,868,120**	**$19,044,359**	**-0.1%**

Real estate tax

The City's real estate tax represents more than one-third of the City's total revenues. For 2019, the City projects approximately $6.6 million will come from this source, including delinquent payments. The City levied a 14.226 mill real estate tax in 2019 that is directed to the General, Debt Service, and Library Funds.

	2019 Tax Rate	Est. Real Estate Tax Revenues
General Fund	11.52	$4,860,577
Debt Service Fund	2.53	$1,080,181
Library Fund	0.177	$74,847
Current Year Revenues	**14.226**	**$6,015,605**
Prior Year Revenues	**N/A**	**$560,000**
Total Revenues	**N/A**	**$6,575,605**

A number of events happened since 2015 that changed how the City projects this revenue. Prior to 2016, the County Tax Claim Bureau collected delinquent taxes on behalf of New Castle and all other Lawrence County municipalities. Based on the Coordinator's recommendation in the 2015 Amended Recovery Plan[14], the City contracted its delinquent real estate tax collection to a third-party collector in 2016. While the intended outcome of that effort was to improve delinquent collections, the practical impact of implementing the initiative was that the collection rate for City's current year taxes improved significantly. The City saw an increase in its current year collections from 84 percent in 2015 to 86 percent in 2016 and another increase to 87 percent in 2017, despite tax increases in both of those years.

Total Current Year Real Estate Tax Revenue

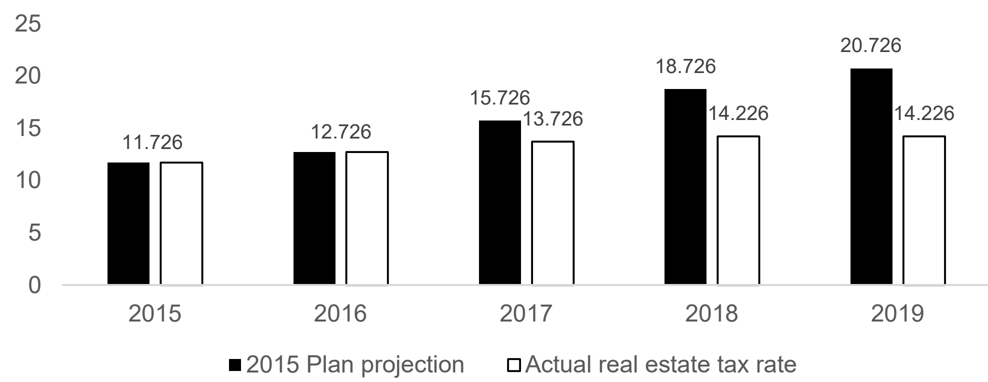
	2011	2012	2013	2014	2015	2016	2017
General Fund	3,904,121	4,702,864	4,692,088	4,551,609	3,715,909	4,491,990	5,011,141
Sinking Fund	708,232	173,422	265,367	181,044	1,048,394	847,826	815,369
Library Fund	71,800	71,945	72,055	73,098	72,640	75,923	69,788
Total	**4,684,153**	**4,948,230**	**5,029,510**	**4,805,751**	**4,836,944**	**5,415,740**	**5,896,298**
Tax Rate (Mills)	**11.726**	**11.726**	**11.726**	**11.726**	**11.726**	**12.726**	**13.726**
Collection Rate	**80.1%**	**84.6%**	**85.6%**	**82.5%**	**83.7%**	**86.2%**	**87.4%**

[14] See initiative RV04 on p. 169 of the 2015 Amended Recovery Plan.

The improved collection rate was counter to the City's historical trends. In 2009, the last tax increase prior to the one in 2016, the City's collection rate dropped from 78 percent to 74 percent. The Coordinator therefore used the same 3:1 ratio (i.e. every three percent increase in the tax rate increase will result in a one percent drop in collections) assumption in the 2015 Amended Recovery Plan and projected that the City's collections rate would drop to 74 percent in 2017 based on the assumed tax rate increase.

Due in part to the City using a third-party delinquent tax collector, the City's current year tax collection rate increased in 2016 and 2017, contrary to the trend in 2009 and the subsequent assumption used in the 2015 Amended Recovery Plan. As a result, the City had lower tax rate increases than described in the Amended Plan in 2017.

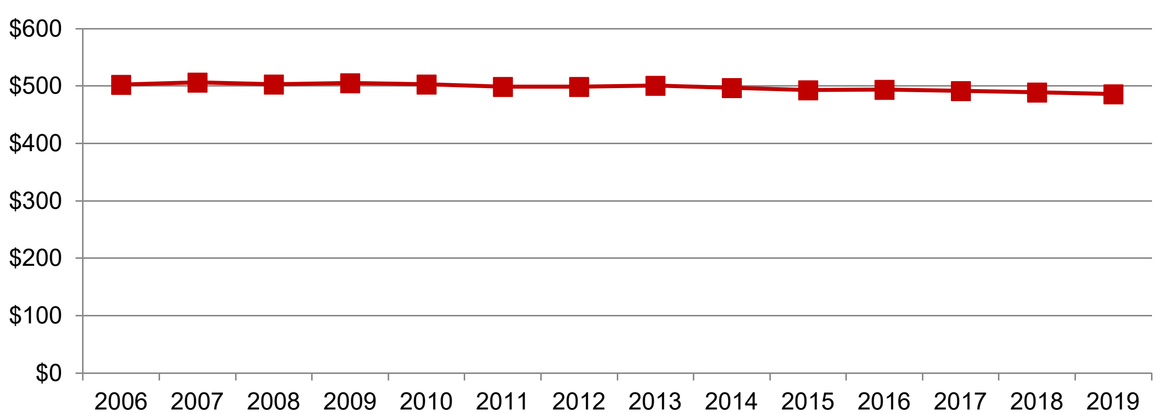
Real estate tax rates, 2015 - 2019



Some of the increase in current year revenues, however, was offset by lower delinquent collections. The City's delinquent collections in 2017 dropped by over 50 percent, likely, in part, because the increased current collection rate in 2016 resulted in lower delinquencies.

In addition to changes to tax rates and the way the City collects its taxes, there were changes to the City's tax base as well. For each of the years from 2013 to 2019, the City saw a decline in its taxable assessed values except in 2016. Compared to 2013, the taxable assessed value in 2019 was 3.0 percent (or $14.9 million) lower. Compared to 2006, the City's 2019 taxable assessed value was 3.3 percent lower.

Taxable Assessed Values, 2006 – 2019 (in millions)



As a result of all of these changes, the City's total real estate revenues increased by 6.6 percent from 2013 through 2017. The following table details the City's current and prior year tax revenues during the five-year period.

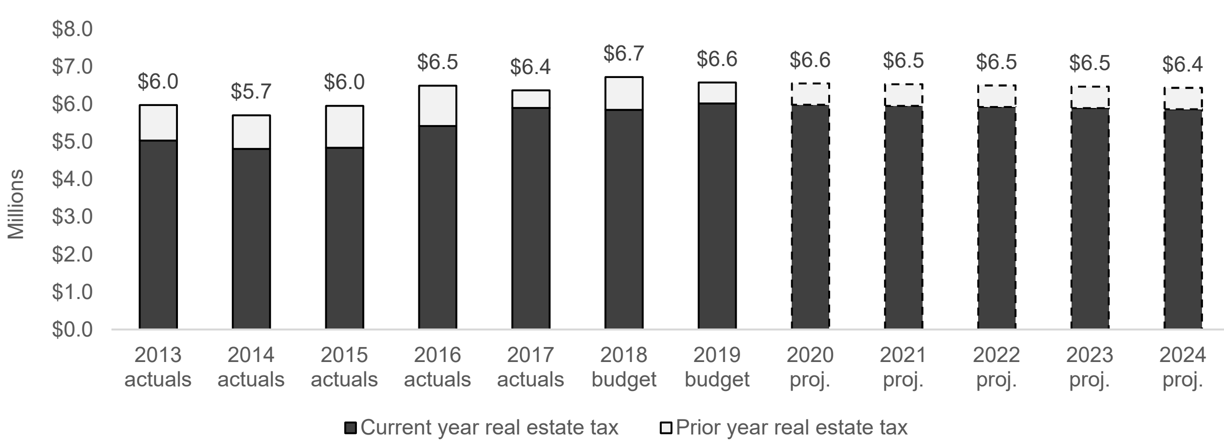
Real estate tax revenues, 2013 - 2017

Taxable assessed values	$500.9	$497.0	$493.0	$493.8	$491.5	
Tax rate	11.726	11.726	11.726	12.726	13.726	
Collection rate	85.6%	82.5%	83.7%	86.2%	87.4%	
Current year revenues	**5,029,510**	**4,805,751**	**4,836,944**	**5,415,740**	**5,896,298**	
Prior year revenues	**943,846**	**898,439**	**1,118,089**	**1,075,659**	**469,710**	

Moving forward, the baseline projection assumes that the real estate tax rate will remain at the current level (14.226 mills) and the taxable assessed value will drop by 0.5 percent annually, consistent with the recent years' trend of declining tax base. Based on these underlying assumptions, current year real estate tax revenue is projected to drop from $6.0 million in 2019 to $5.9 million in 2024.

The City's 2019 budget projects $560,000 in delinquent tax revenues, which is a reasonable estimate given the 2017 results and the recent downward trend. We project the City will continue to collect approximately 20 percent of the prior three years' delinquent taxes, consistent with the 2019 budget assumption, which translates to $566,000 in 2020 growing to $567,000 in 2024.

Historical and Projected Real Estate Tax (All Funds)



	2013 Actuals	2014 Actuals	2015 Actuals	2016 Actuals	2017 Budget	2018 Budget	2019 Budget
General Fund	11.18	11.18	8.969	10.58	11.58	11.52	11.52
Debt Service	0.369	0.369	2.58	1.97	1.97	2.53	2.53
Library	0.177	0.177	0.177	0.18	0.18	0.18	0.18
Total Mileage	**11.726**	**11.726**	**11.726**	**12.726**	**13.726**	**14.226**	**14.226**

Earned income tax

The **earned income tax** is the City's single largest revenue source, representing 36 percent of the City's total operating budget.

The City's adopted 2019 budget anticipates $7.0 million in EIT revenue, including prior year receipts. That revenue flows into the General Fund where it supports daily operations ($3.2 million), the Sinking Fund where it is used to pay pension bond debt service ($1.8 million) and the Pension Fund that the City uses to make its annual contribution to the employee pension plans ($2.0 million).

The City uses three different Pennsylvania laws to levy the EIT:

Authorizing law	Funding purpose	2019 EIT Rate
Act 511 of 1965	Fund daily operations in the General Fund	1.0% Resident (Split with School District) 1.0% Non-resident**
Act 47 of 1987	Fund daily operations in the General Fund	0.2% Resident 0.15% Non-Resident
Act 47 of 1987	Fund capital improvement projects	0.2% Resident 0.15% Non-Resident
Act 205 of 1984	Fund City contribution to employee pension plans (including a portion of the pension bond debt)	0.7% Resident 0.7% Non-Resident
	Total	**2.1% Resident** **2.0% Non-resident**

*** Associated revenue often remitted to the non-resident's home municipality*

At the time when the Coordinator wrote the 2015 Amended Recovery Plan, DCED advised the Coordinator that the Amended Recovery Plan could not presume that the City would subsequently use the three-year exit plan option. Since the objective was for New Castle to successfully exit Act 47 oversight, the Coordinator assumed, at the time, that the Act 47 portion of the resident and commuter EIT tax would need to be eliminated by 2019.

In 2018, DCED advised the Coordinator that the City can keep its Act 47 EIT as long as the City remains under Act 47 oversight. Accordingly, if a three-year exit plan is adopted in 2019, the City would be able to keep its additional taxing authority in Act 47 through 2022, the end of the exit plan period.

The Coordinator developed a Plan Amendment in 2018 that allows the City to keep half of the Act 47 EIT for operations, with the other half directed to capital improvements. The City currently levies a 0.4 percent Act 47 EIT on residents and a 0.3 percent Act 47 EIT on commuters.

If an exit plan is adopted, the City will have to eliminate this Act 47 EIT on residents and commuters by the end of 2022. To help prepare for this eventuality while still providing the necessary capital funding the City needs to maintain its infrastructure, the baseline projection assumes that the City would gradually shift the operations portion of the Act 47 EIT toward capital uses. The receipts from the capital portion of the Act 47 EIT cannot be used to support operations, retire existing debt or cover the City's pension costs, but can provide funding for capital improvement projects such as vehicle replacement, building maintenance, and road paving. Beginning in 2023, the entire Act 47 levy is eliminated in the baseline projection.

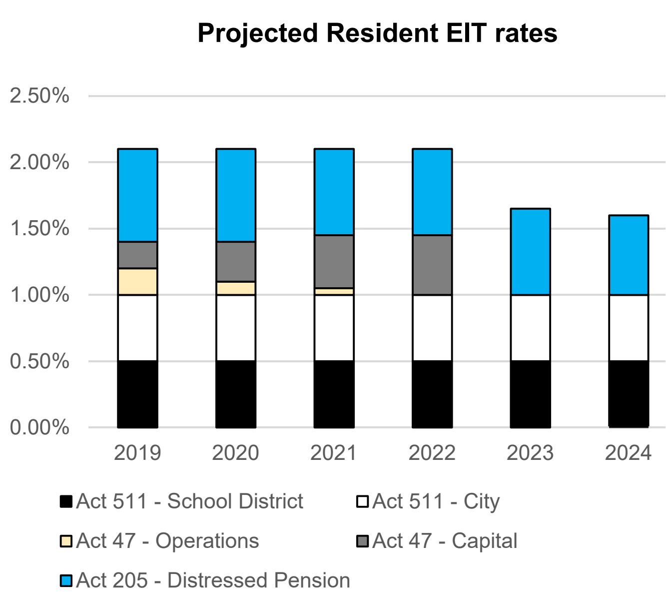
The baseline assumes that the City will continue to use the taxing authority provided by Act 205 to fund a portion of its pension-related expenditures. The Act 205 pension tax rates shown in the below table are only estimates based on the information available at this time. The City will have to calculate the actual distressed pension tax rate each year to incorporate subsequent changes to the relevant factors (e.g. MMO contributions, pensionable payroll, EIT revenue growth). If the distressed pension tax generates more revenue than the City needs for its annual pension costs in any year, then the City will have to use that revenue as an additional contribution to the employee pension plans, over and above the MMO. The City cannot use the additional distressed pension tax revenue to reduce the portion of its pension contribution that has to come from sources other than the pension tax or for purposes unrelated to the pension fund.

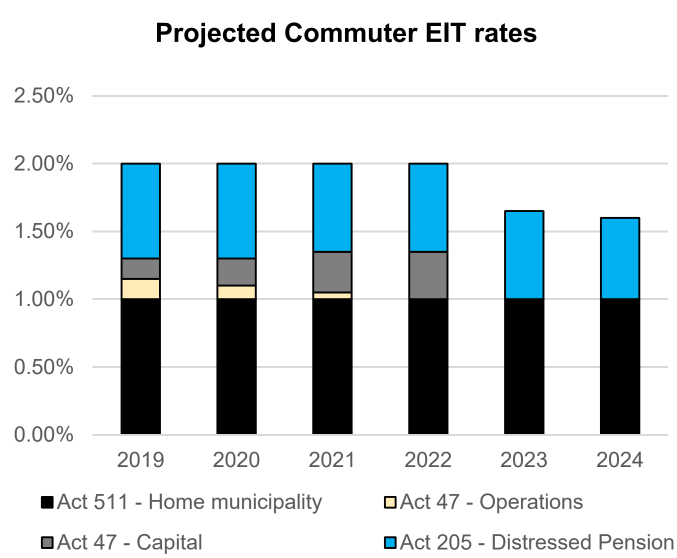
Resident EIT Rate

	2019	2020	2021	2022	2023	2024
Act 511 - School District	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%
Act 511 - City	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%
Act 47 - Operations	0.20%	0.10%	0.05%	0.00%	0.00%	0.00%
Act 47 – Capital (Paving)	0.20%	0.30%	0.40%	0.45%	0.00%	0.00%
Act 205 - Distressed Pension	0.70%	0.70%	0.65%	0.65%	0.65%	0.60%
Total	**2.10%**	**2.10%**	**2.10%**	**2.10%**	**1.65%**	**1.60%**

Non-Resident (or Commuter) EIT Rate

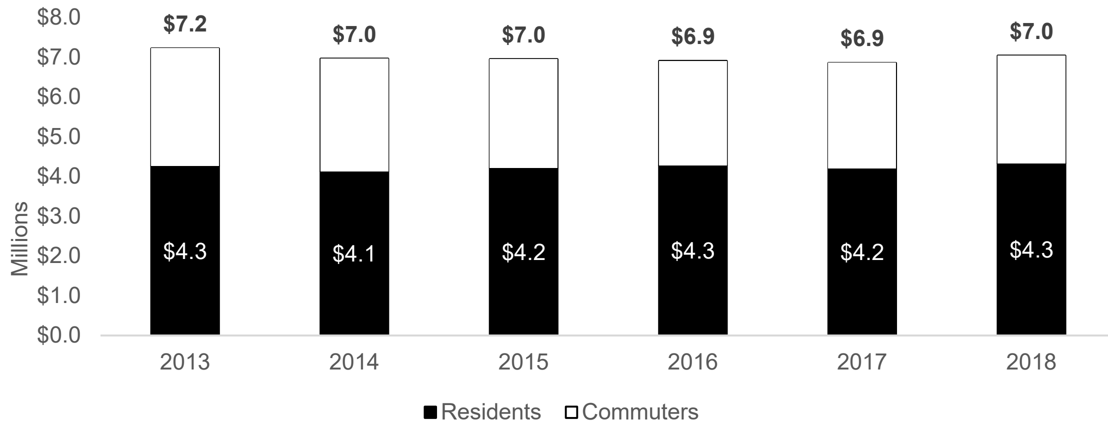
	2019	2020	2021	2022	2023	2024
Act 511 - Home municipality	1.00%	1.00%	1.00%	1.00%	1.00%	1.00%
Act 47 – Operations	0.15%	0.10%	0.05%	0.00%	0.00%	0.00%
Act 47 – Capital (Paving)	0.15%	0.20%	0.30%	0.35%	0.00%	0.00%
Act 205 - Distressed Pension	0.70%	0.70%	0.65%	0.65%	0.65%	0.60%
Total	**2.00%**	**2.00%**	**2.00%**	**2.00%**	**1.65%**	**1.60%**





EIT revenues from residents and commuters dropped from 2013 to 2014, across all payers, by 3.5 percent. Total EIT revenues have been basically flat since 2014, though there was a modest uptick in total revenues in 2018 according to the most recent cash based results.

Total EIT Revenues, 2012 – 2017 (on a cash basis)



Tax base growth has been a little more positive than tax revenue growth. We calculate the amount of revenue each 1.0 percent generates on a cash basis to have a clearer picture of how resident and commuter earnings are changing, once we account for any changes in the tax rate. As noted earlier, the 2015 Amended Recovery Plan anticipated that the City would have to eliminate the Act 47 EIT by 2019 so there was a small tax rate decrease in 2016[15]. The amount of revenue generate per 1.0 percent of EIT increased by 1.9 percent per year for residents and 1.3 percent for commuters from 2015 to 2018.

Revenues per 1.0% in EIT (on a cash basis)

	2013	2014	2015	2016	2017	2018	2013-15 CAGR	2015-18 CAGR
Resident revenues	2,583,915	2,499,679	2,552,147	2,673,090	2,624,817	2,703,110	-0.6%	1.9%
Commuters revenues	2,814,452	2,703,567	2,609,253	2,627,993	2,654,821	2,714,970	-3.7%	1.3%
Total	**$5,398,366**	**$5,203,246**	**$5,161,400**	**$5,301,082**	**$5,279,637**	**$5,418,081**	**-2.2%**	**1.6%**

In addition to reviewing the historical receipts, the Coordinator reviewed economic trend data as a guide for projecting how the resident and commuter tax base will grow. The US Census Bureau's American Community Survey (ACS) tracks New Castle resident's earnings in different ways. As the table below shows, this external data shows growth for most earnings measures, though the pace of that growth varies by indicator. Mean earnings for residents who worked full-time and year-round rose by 3.9 percent per year, but median earnings for residents who are 16 years and over dropped by 0.7 percent annually.

[15] Total EIT for residents dropped from 2.15% in 2015 to 2.10% in 2016 and total EIT for commuters dropped from 2.05% to 2.0% in 2016.

City of New Castle, 2013 - 2017[16]

New Castle	2013	2014	2015	2016	2017	CAGR
Median earnings for people 16 years and over	$25,646	$26,044	$25,143	$25,172	$24,955	-0.7%
Mean earnings for full-time, year-round workers	$39,097	$41,670	$41,781	$42,007	$45,582	3.9%
Per capita income	$17,945	$18,463	$19,206	$19,286	$20,636	3.6%
Median household income	$29,559	$29,762	$30,422	$31,557	$31,044	1.2%

Source: US Census Bureau, American Community Survey, five-year estimates

Another variable in the earned income tax base is whether the number of employed residents has increased. Over the period from 2013 to 2017, the number of employed residents decreased by 1.2 percent on an average annual basis according to the US Bureau of Labor Statistics' Local Area Unemployment Statistics (LAUS).

For commuters, there is federal data available for Lawrence County residents, but the data covers all County residents while the only residents who are relevant to New Castle's commuter tax are those who live outside New Castle but work in the City. The federal data also does not incorporate people from outside Lawrence County who work in New Castle and pay the commuter EIT. With these limitations noted, the table below shows some of the relevant available data points.

Lawrence County, 2013 – 2017

Lawrence County	2013	2014	2015	2016	2017	CAGR
Median earnings for people 16 years and over	27,305	$28,092	$28,669	$29,677	$30,026	2.4%
Mean earnings for full-time, year-round workers	46,595	$47,922	$49,805	$51,642	$54,381	3.9%
Per capita income	22,906	$23,519	$24,450	$25,614	$26,918	4.1%
Median household income	43,546	$43,991	$44,571	$45,764	$47,188	2.0%

Source: US Census Bureau, American Community Survey, five-year estimates

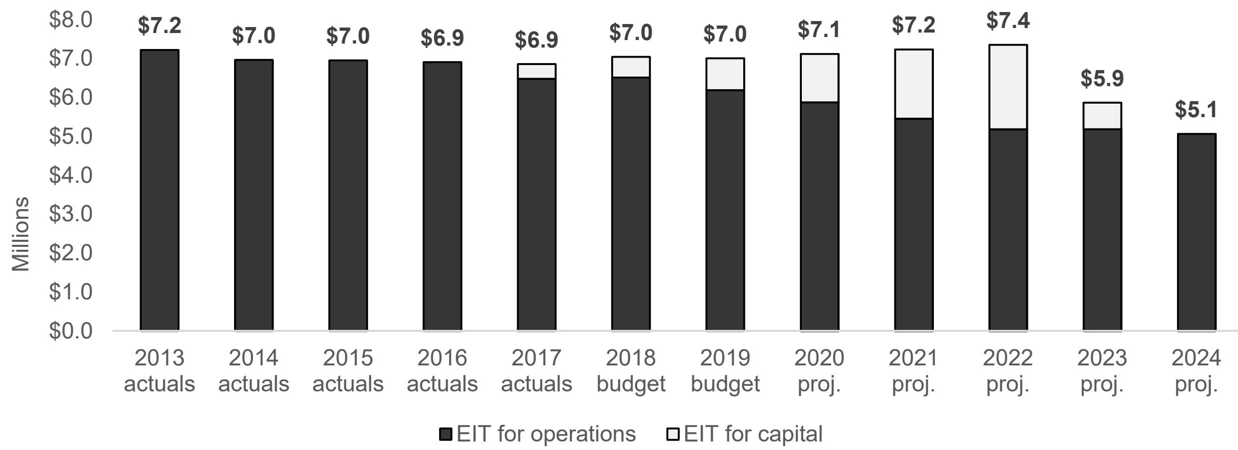
While earnings have generally grown, the number of employed County residents declined during the same period, dropping by 1.1 percent on an annual average basis, according to the US Bureau of LAUS.

Because residents' earnings reported by federal data vary depending on various factors and County residents' earnings data has significant limitations, the Coordinator projected the earned income tax growth based primarily on the City's historical revenue trends. The baseline projection estimates 2.0 percent growth in the resident tax base and a 1.0 percent growth in the commuter tax base based on revenue receipts in the last three years.

The following table shows total historical and projected EIT revenues and the amount designated for capital projects as the City gradually shift its operations Act 47 EIT toward capital uses. In 2023 the City will lose its additional taxing authority provided by Act 47, but there will still be a small amount ($680,000) of prior year revenues available for capital improvement projects from the tax levied in the prior year.

[16] At the time of analysis, the most recent ACS data available was through 2017.

Historical and Projected EIT Revenues (All Funds)[17]



	2019 budget	2020 proj.	2021 proj.	2022 proj.	2023 proj.	2024 proj.
EIT for operations	6,185,552	5,874,837	5,453,817	5,181,442	5,183,880	5,066,005
EIT for capital	817,745	1,242,477	1,779,533	2,170,003	679,968	0
Total	**$7,003,297**	**$7,117,314**	**$7,233,351**	**$7,351,445**	**$5,863,848**	**$5,066,005**

Other taxes

The City projects collecting $1.5 million (or 7.8 percent of the 2019 budget) from other taxes, the largest of which are the local services tax ($430,000) and the business gross receipts tax ($721,000), which includes both the mercantile and business privilege taxes. This category also includes $115,000 in deed transfer tax, which varies depending on the number of residential and commercial property sales.

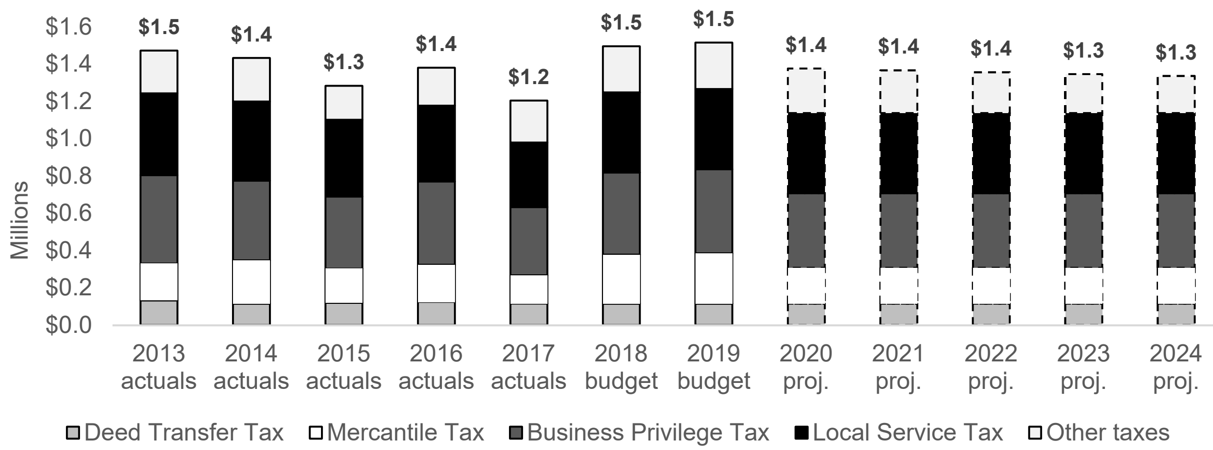
There are other, smaller amounts of tax revenues in the 2019 budget, including payment in lieu of taxes, interest and penalties related to the real estate tax, and delinquent EIT revenue that was due to the City before collection responsibilities shifted to Berkheimer in 2012[18]. These revenues totaled $249,000 in the 2019 budget.

From 2013 to 2017, the other tax revenue category dropped from $1.5 million to $1.2 million, driven primarily by a decline in business gross receipts tax. Based on the actual receipts, the Coordinator adjusted the projection in 2020 for the business gross receipts to the approximate three-year averages from 2015 to 2017. Instead of the $721,000 in anticipated tax revenues in the 2019 budget, the baseline projects $592,000 and maintains the revenue flat throughout the projection period. The Coordinator also reduced the projections for delinquent EIT revenues that was due to the City before collection responsibilities shifted to Berkheimer in 2012. The baseline projection assumes that this revenue will drop from $60,000 in 2019 to $10,000 in 2024 as these revenues are related to older accounts and should gradually decline. All other revenues in this category are projected to be flat for the next five years.

[17] Historical EIT revenues are on a cash basis.

[18] Berkheimer handles delinquent EIT revenue collection for taxes levied in 2011 and later. Sharp handles the older accounts and the City records the revenue as “Collections- Delinquent Tax Receipts,” which is tracked in the “other taxes” category.

Other taxes, 2013 - 2024

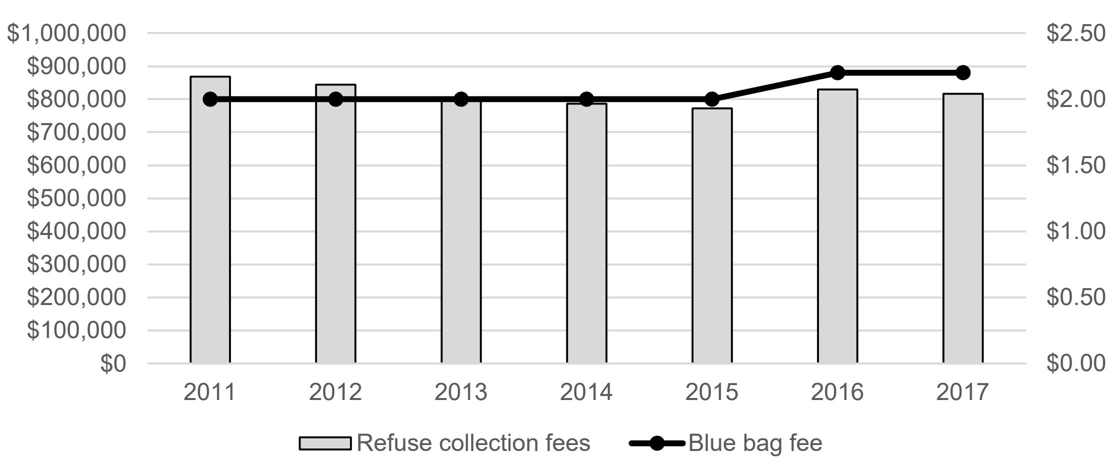


Departmental earnings

Departmental earnings are largely service charges paid by an individual or organization that directly benefits from the service. This category totaled $1.8 million in the 2019 budget and accounts for 8.3 percent of the City's total revenues across the General, Sinking, and Pension funds. Almost half of the departmental earnings come from the City's refuse collection or "blue bag" fees.

The City's refuse collection revenue has been declining since 2011, dropping from $868,000 to $772,000 in 2015. In 2016, the City increased the blue bag fees by 10 percent from $2.00 to $2.20 to recover the cost of the refuse collection program. Revenues as a result increased, but the increase was lower than the fee increase due to the continuous decline in bag sales.

Blue Bag Fee and Refuse Collection Revenues, 2011 - 2017



	2011	2012	2013	2014	2015	2016	2017
Blue bag fee	$2.00	$2.00	$2.00	$2.00	$2.00	$2.20	$2.20
Refuse collection fees	$868,394	$844,031	$803,542	$786,435	$772,362	$829,612	$816,359
% change	N/A	-2.8%	-4.8%	-2.1%	-1.8%	7.4%	-1.6%

The City budgeted $797,000 in blue bag fees in 2019, even though the City has not collected less than $800,000 since the fee increase in 2016. The Coordinator therefore adjusted the projected refuse collection fee to $815,000 in 2020 and maintained it flat for the next five years.

This category also includes employee contributions to health insurance. This revenue fluctuated in recent years in part because of the provision in the 2015 Amended Recovery Plan that capped growth in the City's share of the total premium costs at five percent per year. The baseline projection assumes that the five percent cap continues to apply throughout the projection period, which is discussed more fully in the next section that describes the underlying expenditure assumptions.

Golf course earnings have been growing at an annual rate of 4.8 percent from 2013 to 2017, but the recent years' growth came after years of revenue decline. The baseline projection therefore projects golf course earnings to grow at 2.0 percent based on the historical long-term growth of 2.1 percent from 2011 to 2017.

Code enforcement fees dropped from $205,000 in 2010 to $152,000 in 2013 and have been fluctuating from year to year since then, averaging $171,000 from 2013 to 2017. The City budgeted $188,000 in code enforcement fees in 2019, and the baseline projection assumes it will remain at the 2019 level for the projected years absent fee increases.

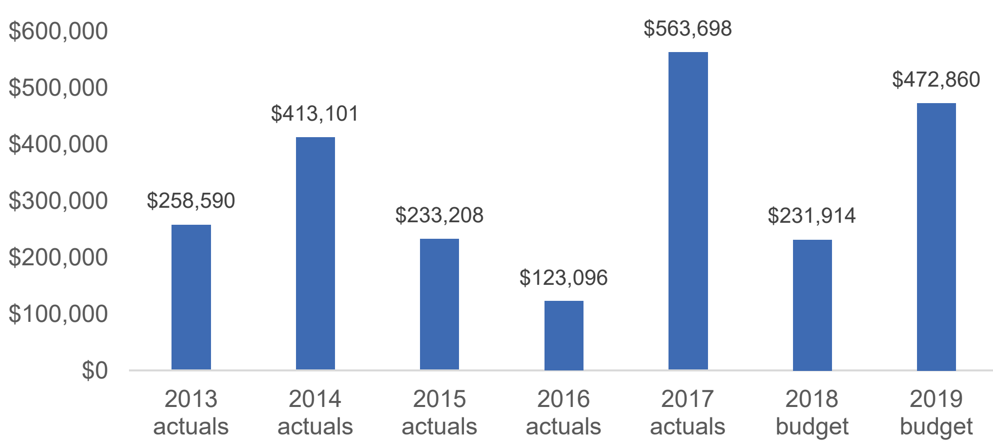
The remaining departmental earnings, which include the water bill fee and security services for Taylor Township and the School District, are all projected to grow at the projected inflationary growth rate of 2.2 percent[19].

Licenses and permits

The City budgeted $839,000 in licenses and permits in 2019, which consist primarily of the building permits and cable access television (CATV) permit revenues. From 2013 to 2017, the City's CATV permit revenues grew from $307,000 to $319,000, or annual average growth of 1.0 percent. The baseline projection therefore continues the historical trends and grow this revenue by 1.0 percent as well.

Building permit revenues have fluctuated depending on the number and scale of construction projects in the City. Part of the building revenues are offset by expenditures because the City contracts with an outside entity for building inspections. The following chart shows the City's building permit revenues from 2013 to 2019.

Buildings Permit Revenues, 2013 - 2019



[19] Q4 2018 Survey of Professional Forecasters published by the Federal Reserve Bank of Philadelphia projects 2.21 percent for the long-term average inflationary growth from 2018 to 2027.

Based on the historical trends and the sporadic nature of this revenue, the Coordinator adjusted 2020 projections to the five-year average revenues from 2013 to 2017 ($318,000) and increased them by 2.0 percent, close to the Federal Reserve Bank's projections for the national gross domestic product (GDP)[20].

Intergovernmental revenues

The largest intergovernmental revenue the City collects is the Commonwealth pension aid, which is recorded in the City's Pension Fund. The amount of aid that New Castle receives is a byproduct of its employee headcount and the amount of revenue that the Commonwealth collects from taxes on out-of-state insurance policies. The Commonwealth aid unit value grew by 3.6 percent on an annual average basis from 2007 to 2017 (10-year average) and by 3.4 percent from 2002 to 2017 (15-year average), so the baseline forecast projects a 3.5 percent growth, assuming headcount remains the same throughout the projection period.

The City also collects a small amount of grants and gifts in the General Fund from the federal, Commonwealth, and County governments. The City budgeted $94,000 in 2019 for grants and gifts, the largest grant of which is a $36,000 grant from the Federal Drug Enforcement Administration. The baseline projection maintains these grants and gifts at the same level as the 2019 budget.

Transfers

This category consists of interfund transfers from special funds to the General Fund. As of 2019, the City has three recurring transfers from other funds:

- **Transfer from liquid fuel**: This allocation from the Commonwealth helps cover street-related expenditures like road paving, road salting, and street lighting. The City budgeted $335,000 in transfers from liquid fuels and the baseline projection assumes that the transfers will remain at the same level.

- **Transfer from CDBG**: The City uses a portion of its federal Community Development Block Grant (CDBG) funding to cover its administrative and code enforcement expenditures. The City also uses a part of its CDBG funding for building demolition. The City budgeted $150,000 in transfer from CDBG in its 2019 budget, and the baseline projection carries that amount forward.

- **Transfer from Parking:** The City also transfers $100,000 from its Parking Fund annually. These are revenues the City receives from the parking meters, surface lots, and North Mercer Street garage. The baseline projection assumes that the $100,000 transfer will follow historical trends and remain flat in the projection period.

The City historically also budgeted a transfer from the Marcellus Shale Gas account that was used to fund capital projects. The Marcellus Shale Gas account held proceeds the City received in 2012 from Hilcorp Energy I, Limited Partnership for leasing its rights to the natural gas on City-owned-properties. That one-time payment was depleted by the end of 2017, so those transfers were not budgeted in 2018 or 2019 and are not included in the baseline projection.

Other revenues

This category includes a number of miscellaneous revenues in the General Fund, including fines and forfeits, school district tax collection fees, and reimbursements from the Commonwealth for pension administration and snow removal. In aggregate, these revenues totaled $397,000 in the 2019 budget and are projected to grow at 0.8 percent annually from $397,000 in 2019 to $412,000 in 2024.

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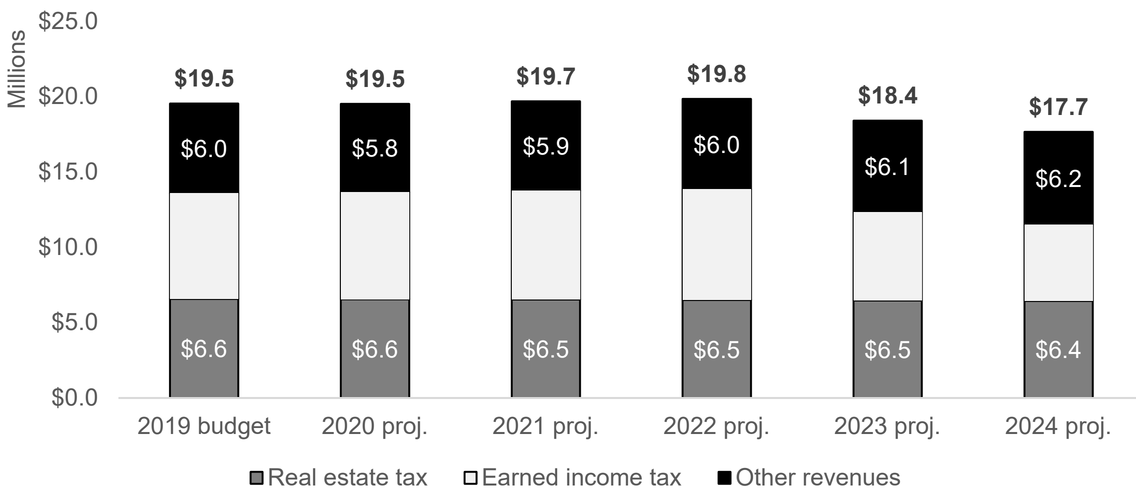
[20] Q4 2018 Survey of Professional Forecasters published by the Federal Reserve Bank of Philadelphia projects 2.1 percent for 2020 and 1.7 perfect for 2021, which averages 1.9 percent.

Summary of revenues

Aggregating all the revenue categories, the baseline projection shows the City's total operating revenues growing by 0.5 percent annually during the period from 2020 to 2022 before dropping to $18.4 million in 2023 when the Act 47 EIT is eliminated as set forth below.

General, Sinking, and Pension Funds' Baseline Projection (Revenues), 2019 – 2024

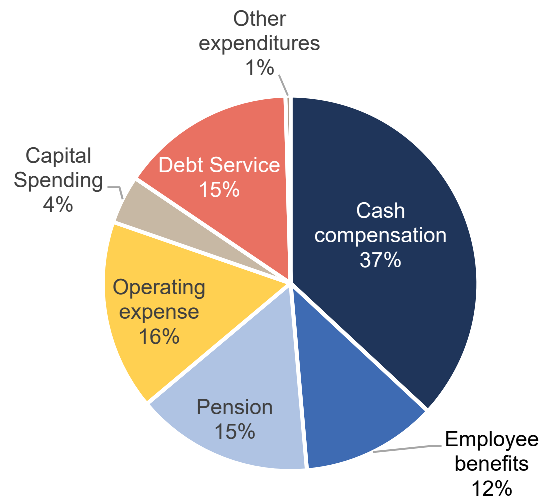


	2019 budget	2020 proj.	2021 proj.	2022 proj.	2023 proj.	2024 proj.	CAGR
Real Estate Taxes	6,575,605	6,552,003	6,531,398	6,498,467	6,465,974	6,433,645	-0.4%
Earned Income Tax	7,003,297	7,117,314	7,233,351	7,351,445	5,863,848	5,066,005	-6.3%
Other Taxes	1,515,144	1,376,566	1,366,566	1,356,566	1,346,566	1,336,566	-2.5%
Licenses and Permits	838,953	691,501	702,149	712,979	723,993	735,195	-2.6%
Departmental Earnings	1,793,064	1,934,344	1,974,394	2,017,406	2,063,650	2,113,911	3.3%
Intergovernmental	835,499	861,455	888,319	916,124	944,902	974,687	3.1%
Other transfers	585,000	585,000	585,000	585,000	585,000	585,000	0.0%
Other Revenues	396,692	399,583	402,537	405,557	408,643	411,796	0.8%
Total Revenues	**$19,543,254**	**$19,517,766**	**$19,683,715**	**$19,843,544**	**$18,402,577**	**$17,656,805**	**-2.0%**

Major expenditure assumptions

Similar to many Pennsylvania local governments, the majority of New Castle's spending is on its employees. In the City's 2019 budget, almost two-thirds of its budget is allocated to employees' cash compensation, health benefits, and the City's contribution to the pension plan. Almost half of the remaining spending goes toward debt service payments, which totaled $3.0 million in the 2019 budget.

2019 Expenditure Budget ($19.5 million)



In aggregate, the City's operating expenditures remained flat at $18.4 million from 2013 to 2017, excluding capital spending which was driven in part by one-time transfers from the Marcellus Shale gas proceeds. The growth in pension contributions was offset by lower debt service and employee benefit costs.

The pie chart to the right shows the major categories of expenditures in the adopted 2019 budget, and the table below shows the City's operating expenditures, including the General, Sinking, and Pension Funds, from 2013 to 2017.

Expenditures across the General, Sinking, and Pension Funds, 2013-2017

	2013 audit	2014 audit	2015 audit	2016 audit	2017 audit	CAGR
Cash compensation	6,921,323	7,154,914	7,219,669	6,973,744	6,933,886	0.0%
Employee benefits	2,607,049	2,830,402	2,820,295	2,219,244	2,268,156	-3.4%
Pension	1,986,457	2,354,001	3,005,567	2,998,155	3,013,273	11.0%
Operating expenses	3,199,542	3,051,577	3,151,535	3,067,135	3,125,305	-0.6%
Capital Spending	371,253	408,417	1,619,151	954,854	461,269	5.6%
Debt Service	3,575,065	2,636,227	2,354,784	2,296,840	2,956,133	-4.6%
Other expenditures	90,219	82,696	79,002	86,223	97,796	2.0%
Total	**$18,750,908**	**$18,518,234**	**$20,250,003**	**$18,596,195**	**$18,855,818**	**0.1%**
Expenditures excl. capital	**$18,379,655**	**$18,109,817**	**$18,630,852**	**$17,641,341**	**$18,394,549**	**0.0%**

Cash compensation

This category includes employees' base salaries, longevity, holiday pay, incentive payments, clothing allowance, shift differential, and overtime. Since adopting the 2015 Amended Recovery Plan, the City has negotiated new collective bargaining agreements with its four bargaining units – the Fraternal Order of Police (FOP), International Association of Firefighters (IAFF), Laborers, Local No. 964 – Public Works, and Laborers, Local No. 964 – Clerical. All of the bargaining agreements complied with the Amended Recovery Plan provision, and are all set to expire at the end of 2019.

Employee Group Contract Term and Headcount

Group	Covered positions include	2019 budgeted positions	Contract term
FOP, Lodge 21	All full-time police officers except the Chief	36	1/1/16 - 12/31/19
Laborers, Local No. 964 - Public Works	Laborers, equipment operators, refuse collectors, tradesmen	23	1/1/17-12/31-19
IAFF, Local No. 180	All full-time fire fighters except the Chief	20	1/1/17-12/31-19
Laborers, Local No. 964 - Clerical	Most clerical and administrative support positions including treasury and records clerks and financial and legal assistants	10	1/1/17-12/31-19
Non-represented[21]	Department directors, elected officials, code officers, part-time employees including police and fire	18 full-time 37 part-time	N/A
Total		**107 full-time 37 part-time**	

From 2015 to 2019, employee cash compensation remained flat even though employees received either annual wage increases of 2.0 percent or one-time bonuses in each of those years. Part of the reason cash compensation growth was lower than the annual wage increases is because the City eliminated positions to control expenditure growth.

Between 2015 and 2018, the City eliminated the economic development direction position, one firefighter position, and one code officer position. Since the establishment of the stormwater fee, the sewer vactor operator position was moved to the Sanitation Authority. As of 2019, the City has 107 full-time positions and 37 part-time positions.

Full-time and Part-time Headcount

	2015	2016	2017	2018	2019
Full-time employees	110	112	107	106	107
Part-time employees	41	36	38	41	37
Total	**151**	**148**	**145**	**147**	**144**

The second reason for the flat cash compensation trend was because the City reduced overtime spending in the Fire Department. During the most recent round of labor negotiations, the City and IAFF agreed that, while the minimum manning level of on-duty firefighters continues to remain at five, part-time firefighters shall be counted toward that minimum manning level. Part-time firefighters previously were not counted toward the five-person minimum. In part due to this new provision, Fire Department overtime dropped from $242,000 in 2015 to $192,000 in 2017, representing a 20.6 percent decrease. The City also saw savings from turnover in recent years, particularly in the Clerical and Public Works union.

As a result of these efforts, the City was able to maintain its total cash compensation at $7.2 million according to the 2019 budget, the same amount the City spent in 2015.

[21] Teamsters, Local 26 is now grouped with non-represented employees.

Total Cash Compensation, 2015 - 2019

	2015 actuals	2016 actuals	2017 actuals	2018 budget	2019 budget
Salaries and Longevity	6,169,718	6,004,667	6,009,004	6,346,436	6,363,012
Other Cash Compensation	506,754	450,529	478,998	482,428	437,963
Overtime	543,197	518,548	445,884	444,542	441,084
Total Cash Compensation	**$7,219,669**	**$6,973,744**	**$6,933,886**	**$7,273,406**	**$7,242,059**

Looking forward, the baseline projection assumes headcount to stay at the 2019 budgeted level over the five-year period. All employees, apart from elected officials, are projected to receive annual across-the-board wage increases of 2.0 percent after the bargaining agreements expire at the end of 2019. The projection also assumes that police officers and firefighters who are not already at the maximum step will continue to receive step increases.

Employee benefits

This category includes the City's benefits payments, which consist of health and life insurance, Social Security, Medicare, unemployment compensation, and workers' compensation. Health insurance spending for both the City's active employees and retirees represents over 70 percent of the spending in this category. From 2015 to 2017, the City's health insurance expenditures net of the employees' contribution dropped from $2.2 million to $1.7 million and the City projected net healthcare costs to grow at an annual rate of less than one percent in 2018 and 2019[22].

Health Insurance Cost, 2015 - 2019

	2015 actuals	2016 actuals	2017 actuals	2018 budget	2019 budget
Gross health insurance (active employees)	$2,066,078	$1,654,393	$1,584,825	$1,631,403	$1,520,297
Gross health insurance (retirees)	$338,772	$212,775	$301,232	$325,608	$351,832
Employee contributions (revenues)	$202,776	$52,885	$153,826	$218,305	$113,685
City net cost	**$2,202,074**	**$1,814,282**	**$1,732,231**	**$1,738,706**	**$1,758,444**

The decrease in health benefit costs was, in part, because all bargaining units were subject to the maximum City contribution (or "cap") beginning in 2017[23]. As described in the Amended Recovery Plan, the Coordinator calculated the maximum City contribution based on the premiums of the United Health plan provided through TEC Benefits in 2015. Because the premiums for this health plan were much lower than the Highmark Plan that fire and police employees were previously using, the Coordinator lowered the "cap" to reflect the premiums at the time.

Maximum City Monthly Contributions, 2015 - 2017

	2015	2016	2017
Single	$524	$551	$480
P/C	$1,187	$1,246	$957
H/W	$1,334	$1,401	$1,011
Family	$1,418	$1,489	$1,251

[22] Part of the reason health insurance growth was lower than projected was because the City now has fewer employees and has more employees who elect not to use City health insurance coverage and opt to receive an annual payment of $2,500 "in lieu of" coverage. This year, there are 23 employees who opted to receive "in-lieu" payments, compared to only 12 employees in 2015.

[23] See initiative WF02 on p. 67 of the 2015 Amended Recovery Plan.

In addition, the City now has fewer employees and employees have switched health plans since the 2015 Plan that has resulted in lower employee contributions as well as lower premium cost for the City. The following table shows monthly premiums of family plans by bargaining unit from 2014 to 2018[24].

Premium for Family Plans (inclusive of health plan changes), 2014 - 2018

	2014	2015	2016	2017	2018
Police	$1,849	$764	$1,179	$1,339	$1,411
Fire	$1,849	$764	$1,271	$1,339	$1,411
Non-union	$1,849	$764	$1,179	$1,339	$1,411
Clerical	$1,824	$1,827	$1,090*	$1,356*	$1,166*
Public Works	$1,824	$1,827	$1,297*	$1,415*	$1,290*

**These are average premiums for family plans because the premiums are employee-based and vary among employees*

The baseline projects gross health premiums to grow at 7.0 percent annually based on the national health trend survey published by Segal Consulting[25]. The baseline also assumes the current cap on the City's growth in premium costs remains at five percent a year.

Pension

The City has three employee pension plans that are funded through a combination of City contributions, employee contributions and plan asset investment earnings. Part of the City's contribution is funded by Commonwealth pension aid, which is reflected in the City's budget as a revenue. These contributions fund a level of benefits defined by the pension plan provisions, irrespective of the investment performance, pension plan funding levels, or other factors used to calculate the City's annual required contribution to the pension plans.

The City's contribution, also known as the Minimum Municipal Obligation (MMO), is calculated by an independent actuary. Every other year the actuary calculates the MMO based on several factors including the pension plan's provisions, the City's payroll, employee contributions, recent investment performance and actuarial assumptions involving factors like life expectancy. The MMO has three components:

- The **normal cost** is the amount that the City has to contribute to cover the value of benefits provided to employees in the current year. It is based in part on the size of the City's current payroll.
- The **amortization component** is the amount the City has to contribute to cover the unfunded liability from prior years' service. This is the largest component of the MMO.
- The **administrative expense** is the anticipated cost of running the pension plan.

The MMO calculation also takes into account the employee contributions to the pension plans. Employees contribute a percentage of their earnings as determined through negotiation and law.[26]

After increasing by an annual rate of 21.0 percent from 2010 to 2015, the City's MMO have stabilized since 2016, and, according to the most recent actuarial valuation, the funding ratio for the Police and Fire

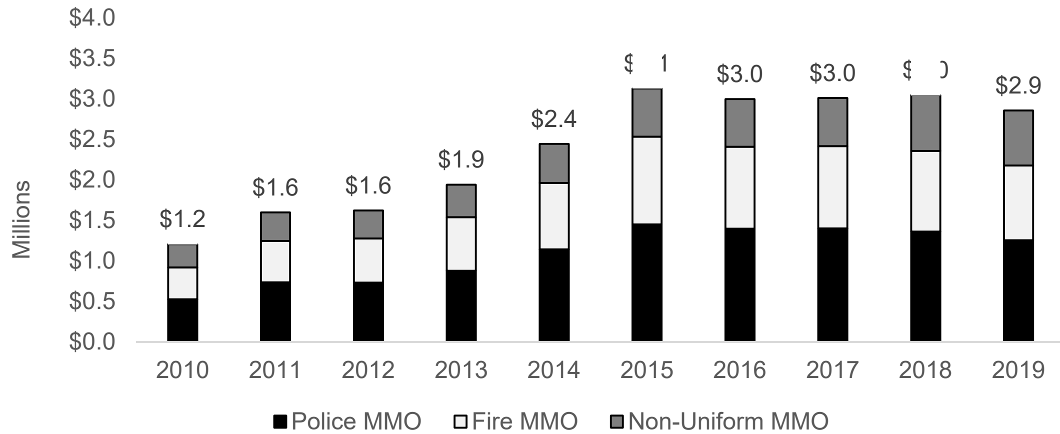
[24] Renewals for police, fire, and non-represented employees are in September; renewals for the clerical and laborer bargaining units are in August.

[25] The 2019 Segal Health Trend Survey projects that high-deductible health plans (HDHPs) will grow at 7.2 percent and PPO and POS plans will grow at 7.1 percent to 7.3 percent depending on the accessibility.

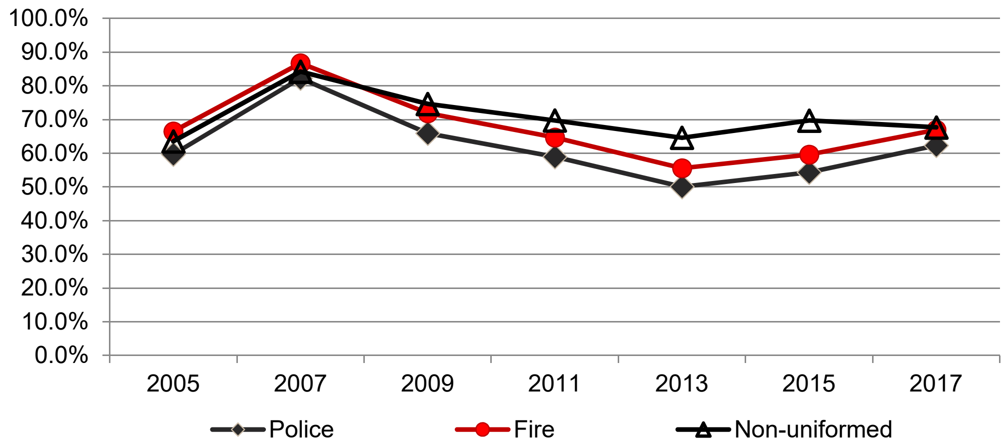
[26] The earnings upon which the employee contributions are based vary by bargaining unit and hiring date. For example, police officers hired before 2013 contribute 4.5 percent of their base salary, longevity and holiday pay. Those hired after 2012 contribute 5.0 percent of their base salary and longevity.

Departments have increased to 62.3 and 66.9 percent respectively. The funding ratio of all three pension plans in aggregate was 65.2 percent as of January 1, 2017, which is considered moderately distressed based on the levels of distress set forth in Act 205.[27]

Actual and Budgeted Minimum Municipal Obligations, 2010 -2019



Funding Ratio, 2005 - 2017



Moving forward, the City's actuary projects that the City's Minimum Municipal Obligation will remain relatively flat at $2.9 million based on data and results from the January 1, 2017 valuation and actual 2019 MMO. The MMO projections as shown in the chart below are included in the baseline projection and do not assume any future experience gains or losses.

Minimum Municipal Obligation projection, 2019 – 2024

	2019	2020	2021	2022	2023	2024
Police	1,254,170	1,285,000	1,301,000	1,318,000	1,335,000	1,353,000
Fire	923,287	942,000	951,000	953,000	962,000	791,000
Other	678,496	671,000	678,000	611,000	637,000	644,000
Total Projected MMO	**$2,855,953**	**$2,898,000**	**$2,930,000**	**$2,882,000**	**$2,934,000**	**$2,788,000**

[27] Act 205 established that funded status of 70 to 89 percent is considered minimally distressed; funded status of 50 to 69 percent is considered moderately distressed; and funded status of less than 50 percent is considered severely distressed.

Operating expense

The City anticipates spending $3.2 million (or 16.4 percent) of the 2019 budget on operating expenses, which include contracted services, materials, supplies, and utilities. From 2013 to 2017, the City's annual operating spending essentially remained the same, despite inflationary growth of 5.2 percent through that period[28].

Operating Spending, 2013 - 2017

	2013 actuals	2014 actuals	2015 actuals	2016 actuals	2017 actuals	CAGR
Contracted services	1,561,779	1,343,537	1,493,423	1,528,305	1,506,275	-0.9%
Utilities	1,018,018	1,014,228	946,556	888,089	919,682	-2.5%
Materials and supplies	619,745	693,813	711,556	650,742	699,348	3.1%
Total operating expense	**$3,199,542**	**$3,051,577**	**$3,151,535**	**$3,067,135**	**$3,125,305**	**-0.6%**

The largest spending in this category is contracted services, which includes the City's contracts for building inspections, refuse bag packaging, and engineering services. It also includes tipping fees for waste disposal, contracted vehicle repairs, and the City's annual contribution to the New Castle Area Transit Authority.

With a couple of noteworthy exceptions, the baseline projection assumes that most operating expenses will increase according to the inflationary growth of 2.2 percent projected by the Survey of Professional Forecasters. Landfill tipping fees are projected to grow by 5.0 percent, matching the rate of historical spending from 2011 to 2017. Based on the long-term projections by the US Energy Information Administration, the baseline forecast projects vehicle gasoline costs to grow at 3.6 percent and electricity to grow at 2.5 percent annually. The City's recycling fee increased from $68.5 per ton to $150 per ton this year and the City is now exploring alternative ways to recover its costs. The Coordinator will revisit this particular expenditure and may update the projections in the Exit Plan.

Capital spending

Since entering Commonwealth oversight in 2007, the City has rarely issued new debt to fund capital improvements and has generally done so only if there are other debt-related transactions occurring simultaneously. For example, when the City refunded its pension obligation bonds in early 2015, it did a second, much smaller issuance of $355,000 to help purchase a new fire truck.

Since the City cannot afford to issue large amounts of new debt, it has relied on a "pay-as-you-go" approach to funding capital projects, largely from the following sources:

- **Marcellus Shale funds:** In 2012, the Mayor signed an agreement to lease the rights to the natural gas on City-owned properties to Hilcorp Energy I, Limited Partnership. In return, the City received a one-time payment of $1.8 million, which the City used for capital improvement projects from 2014 to 2016; and

- **One-time EIT windfall:** In 2014 the City closed an old account established years before New Castle entered Act 47, when the Treasurer's Office collected earned income tax from residents and non-residents who worked in the City. Closing that account resulted in a $980,000 transfer into the General Fund, which the City used for capital projects after the Marcellus Shale gas proceeds were exhausted.

[28] CPI-All Urban Customers, Bureau of Labor Statistics

The City also receives liquid fuels revenue for street-related projects, such as paving, and has used grants and donations to supplement its capital budget. Since 2017, the City has relied on a portion of the Act 47 EIT for capital projects according to the provisions in the 2016 and 2018 Plan Amendments.

As stated in the revenue section of this chapter, the baseline projection assumes that the City would gradually shift the operations portion of the Act 47 EIT toward capital uses. This shift should provide some funding for the City's capital improvement projects, including vehicle replacements, building maintenance, and road paving. The baseline forecast projects that the Act 47 capital EIT levy will provide revenues growing from $818,000 in 2019 to $2.2 million in 2022. Beginning in 2023, the City will lose its additional taxing authority provided by Act 47, but there will still be a small amount ($680,000) of prior year revenues available for capital improvement projects from the Act 47 levy in the prior year.

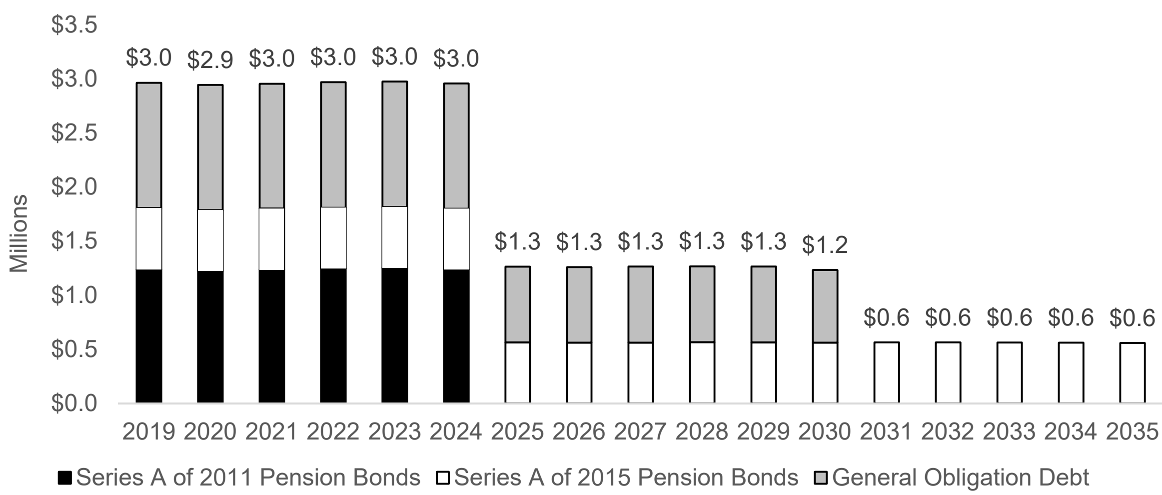
Act 47 Capital EIT

Resident Act 47 Capital EIT	0.20%	0.30%	0.40%	0.45%	0.0%	0.0%
Commuter Act 47 Capital EIT	0.15%	0.20%	0.30%	0.35%	0.0%	0.0%
Capital EIT Revenues	**$817,745**	**$1,242,477**	**$1,779,533**	**$2,170,003**	**$679,968**	**$0**

<u>Debt service</u>

The baseline projection follows the City's existing debt schedule and does not assume any new borrowing for the next five years. According to the existing debt schedule, the City's debt service will remain at approximately $3.0 million annually for the next five years. The City is currently exploring refinancing opportunities that may reduce debt service spending over the next five years. The Exit Plan will include updates to the projection if the City refinances its debt.

Existing Debt Schedule, 2019 - 2035



According to the existing debt schedule, debt service payments will remain at $3.0 million through 2024, after which they will drop to $1.3 million since the City would have paid off the Series A of 2011 Pension Bonds and the General Obligation debt would drop from $1.2 million to $700,000.

Because the City uses the distressed pension (Act 205) EIT to pay for the majority of the pension bonds and, according to Act 205, the City can only use the revenue from this distressed pension tax to pay its pension obligation bond debt or make its annual MMO payments to the employee pension plans, its earned income tax revenues will drop in 2025, in tandem with the drop in pension bond payments. Practically speaking, the City's revenue will drop by $1.2 million in 2025 (equivalent to the debt service related to the series A of 2011 Pension Bonds) while expenditures will drop by $1.7 million according to the existing debt schedule.

Other expenditures

This category includes the contribution to the library and few other miscellaneous expenditure line items. As mentioned earlier in the revenue section of this chapter, the City levies a 0.177 mill Library Fund real estate tax. The City collects the revenue and passes it through to the New Castle Public Library. The annual contribution to the Library is recorded in this category, and is projected to drop by 0.5 percent annually based on the projected decline in taxable assessed value. The current levy of 0.177 mill is projected to remain flat throughout the projection period.

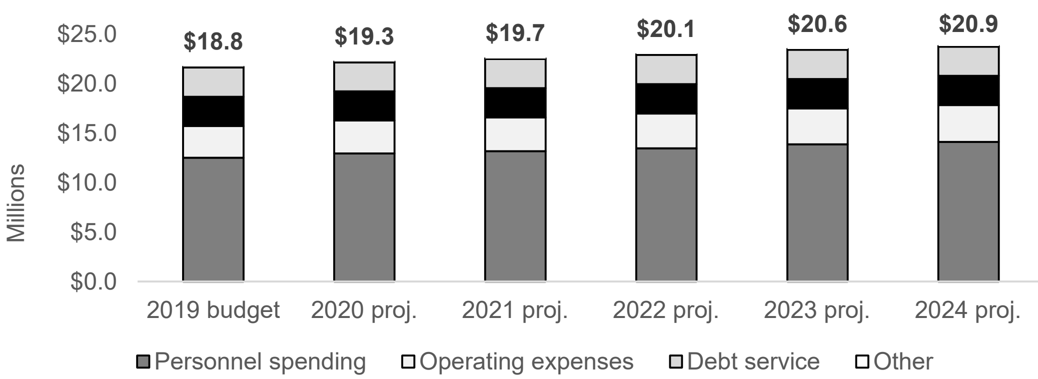
Library Contribution

	2019 budget	2020 Proj.	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
Library levy	0.177 mills	0.177 mills	0.177 mills	0.177 mills	0.177 mills	0.177 mills
Library contribution	$74,847	$74,473	$74,100	$73,730	$73,361	$72,994

Summary of expenditures

Aggregating all expenditure categories, the baseline projection shows the City's total operating expenditures (excluding capital spending) growing by 2.1 percent annually from $18.8 million in 2019 to $20.9 million in 2024.

General, Sinking, and Pension Funds' Baseline Projection (Operating Expenditures), 2019 – 2024

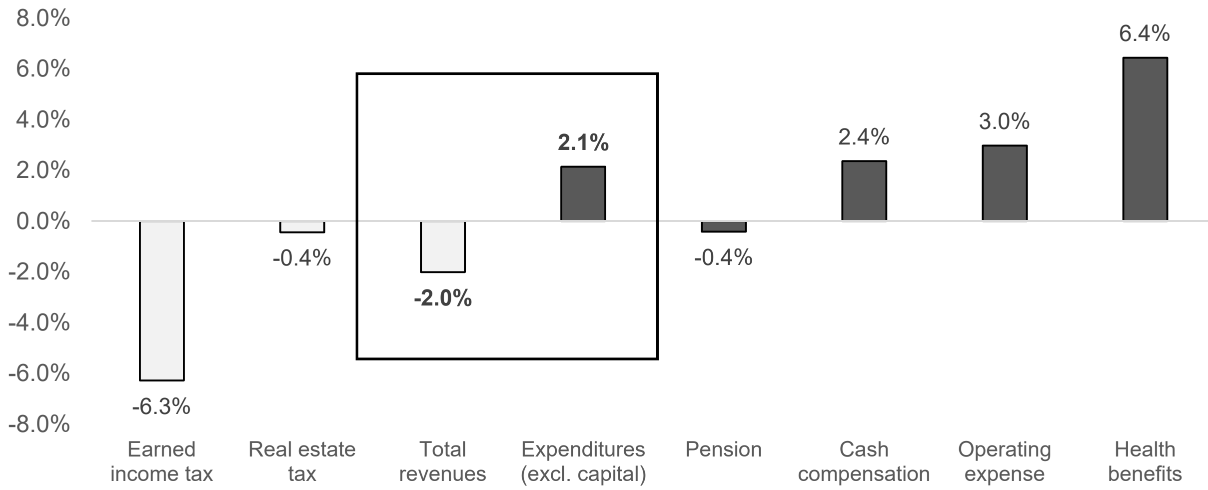


	2019 budget	2020 proj.	2021 proj.	2022 proj.	2023 proj.	2024 proj.	CAGR
Cash compensation	7,242,059	7,432,832	7,619,649	7,791,998	7,969,442	8,141,604	2.4%
Employee benefits	2,292,404	2,517,142	2,641,425	2,773,194	2,912,670	3,060,772	6.0%
Pension	2,995,783	3,032,147	2,937,292	2,928,643	3,021,839	2,934,263	-0.4%
Operating expense	3,217,856	3,325,647	3,421,116	3,519,706	3,621,534	3,726,718	3.0%
Capital Spending	817,745	1,242,477	1,779,533	2,170,003	679,968	0	-100.0%
Debt service	2,962,337	2,941,899	2,953,173	2,966,986	2,972,764	2,955,894	0.0%
Other expenditures	83,347	83,144	82,948	82,758	82,577	82,402	-0.2%
Total	**$19,611,533**	**$20,575,288**	**$21,435,137**	**$22,233,288**	**$21,260,793**	**$20,901,653**	**1.3%**
Expenditures excl. capital	**$18,793,788**	**$19,332,811**	**$19,655,603**	**$20,063,285**	**$20,580,825**	**$20,901,653**	**2.1%**

Major budget drivers

For the five-year period from 2020 to 2024, revenues are projected to decline by at an annual average rate of 2.0 percent driven largely by the elimination of the Act 47 EIT and the continued decline in taxable assessed values, while operating expenditures are projected to increase at an annual average rate of 2.1 percent driven largely by personnel expenses. The following chart highlights key revenue and expenditure budget drivers across the baseline projection period.

Major Budget Drivers – Compounded Annual Growth Rate (CAGR), 2019 - 2024



	2019	2024	Change ($)	CAGR
Earned income tax	$7,003,297	$5,066,005	($1,937,292)	-6.3%
Real estate tax	$6,575,605	$6,433,645	($141,961)	-0.4%
Total Revenues	**$19,543,254**	**$17,656,805**	**($1,886,449)**	**-2.0%**
Expenditures (excl. capital)	**$18,793,788**	**$20,901,653**	**$2,107,866**	**2.1%**
Pension	$2,995,783	$2,934,263	($61,520)	-0.4%
Cash compensation	$7,242,059	$8,141,604	$899,545	2.4%
Operating expense	$3,217,856	$3,726,718	$508,861	3.0%
Health benefits	$2,029,193	$2,771,892	$742,699	6.4%

As shown in the table and chart above, the City is projected to have a deficit over the next five years as a result of declining revenues and growing expenditures. The City's revenues are projected to drop by an annual rate of 2.0 percent due primarily to the elimination of the Act 47 EIT and an eroding tax base. Operating expenditures, on the other hand, are projected to grow at 2.1 percent annually even if the City provides two-percent across-the-board wage increases and health insurance growth is capped at five percent. Beyond this challenge, the City also needs to find alternative funding for capital improvements once the Act 47 EIT is eliminated after 2022.

The next chapter highlights the major challenges the City is expected to have to tackle over the next three years to bolster its chance to exit Act 47 oversight.

Major Challenges

The City has made progress since entering Act 47 in 2007, but more must be done in order for New Castle to achieve long-term financial recovery. While one of the New Castle's biggest challenges is its demographic weaknesses that are largely beyond the City's control, New Castle can still make progress toward financial recovery in areas where it has control, such as aligning growth in expenditures with the growth in the revenues available to pay for them. This chapter highlights the major challenges the City will have to address within the next three years to bolster its ability to exit oversight by the end of 2022.

Revenues

As detailed in the baseline projection chapter, the City's revenues are projected to drop from $19.5 million in 2019 to $17.7 million in 2024 primarily because of the phasing out of the Act 47 EIT. But even without the elimination of the additional taxing authority, the City would still struggle with an imbalance where expenditure growth outpaces revenue growth.

From 2013 to 2017, the City's tax revenues, which represent more than three-quarters of the City's total revenues across the General, Sinking, and Pension Funds, declined by 0.2 percent on an annual average basis despite real estate tax rate increases in 2016 and 2017. As shown in the table below, apart from the real estate tax, almost all of the City's tax revenues decreased in the last five years. Absent the real estate tax increases, the City's real estate tax revenues would have dropped as well with taxable assessed values decreasing by 1.9 percent from $500.9 million in 2013 to $491.5 million in 2017.

Tax Revenues from 2013 - 2017

	2013	2014	2015	2016	2017	2013-17 CAGR
Real Estate Taxes	5,973,356	5,704,190	5,955,032	6,491,399	6,366,008	1.6%
EIT (on a cash basis)	7,218,634	6,963,216	6,950,759	6,904,936	6,854,527	-1.3%
Business Gross Receipts Tax	671,781	659,766	570,342	646,173	516,686	-6.4%
Local Services Tax	438,767	424,159	411,831	407,184	445,674	0.4%
Deed transfer tax	132,329	115,072	119,226	123,882	116,043	-3.2%
Other taxes	229,411	233,763	181,677	203,526	225,154	-0.5%
Total tax revenues	**$14,664,277**	**$14,100,166**	**$14,188,868**	**$14,777,100**	**$14,524,093**	**-0.2%**

While controlling expenditure growth is essential to maintaining fiscal balance, the City must also find ways to grow its revenues to fund expenditure growth, especially if the City wants to keep employees' wages competitive. Because of the declining tax base and the limited options available to the City, the exit plan will likely include proposed increases to the current tax rate unless the City finds alternative ways that can generate revenues or savings large enough to cover the projected deficits as shown in the baseline projection.

Economic development

True, long-term financial recovery means more than balancing revenues against expenditures on an annual basis, though that is a core component of it. New Castle's primary taxes are the real estate tax and the resident earned income tax, so the City needs growth in the total assessed value of property in the City and resident earnings.

Since 2015, the City has made some progress in advancing its economic development goals. The following highlights the progress the City has made since 2015:

- The Mayor appointed a Blighted Property Task Force and developed a comprehensive blight strategy plan through a grant provided by DCED, which includes recommendations such as forming a land bank, developing strategies for targeted demolitions, increasing the focus on code enforcement, and repurposing blight properties to productive use.

- The City is partnering with *10,000 Friends*, a Pennsylvania non-profit that advocates for responsible and efficient land use, to administer the Southside redevelopment plan. The redevelopment program, which is supported by DCED's *Neighborhood Partnership Program* (NPP), includes blight removal, business district investment, clean-up activities, human services expansion, housing rehabilitation, parks improvements, and law enforcement coordination through the District Attorney's office.

- The City established a Community Development Corporation (CDC) in 2018 to take advantage of the *Neighborhood Partnership Program* administered by DCED and to provide a focus for the central business district. The CDC works closely with the City Council and the Blueprint Community members to bring a focused community strategy for advancing economic development projects.

- The City is in active negotiations to purchase the former *Shenango China Plant* property with support from an Environmental Protection Agency (EPA) brownfields grant administered by the Lawrence County Community Development Corporation (LCCDC).

While the City has indeed advanced some of the economic development initiatives proposed in the 2015 Amended Recovery Plan, more must be done in order to help stabilize and grow the City's declining tax base.

The 2015 Amended Recovery Plan also discussed how code enforcement is closely tied to economic development, since one of the Code Department's main responsibilities is to reduce the number of blighted and vacant properties to address health and public safety concerns, improve the quality of life for residents, stabilize property values, and enhance New Castle's ability to attract and retain residents and businesses. Since 2017, the Coordinator has been issuing quarterly code enforcement performance reports that track the Department's performance in three areas:

- Workload measures including the number of open cases, complaints received, etc.;

- Productivity measures including the number of inspections completed, violations issued, etc.; and

- Effectiveness measures including the number or percent of houses in compliance with code, cleanliness of City neighborhoods, etc.

While the efforts and compiling the necessary data are still a work in progress, the data provided in these reports shed light on the quality of the housing stock in New Castle and areas that need improvement in the Department's operations. The exit plan will provide strategies to help the City improve its code operations using data measured in the quarterly performance reports.

Workforce

In recent years, the City has suggested that employee compensation may not be competitive in the current economic environment and requested additional wage increases for selected employees. The Coordinator advised the City to comply with the collective bargaining agreements and revisit the issue during labor negotiations in 2019.

The Coordinator recognizes that compensation can be an important factor in the City's recruitment and retention of its employees. At the same time, there is a fundamental tension that exists between the desire to increase employee wages beyond cost-of-living adjustments and the financial realities described throughout this Report. For the City to afford regular cost-of-living increases to all its employees and to give itself a chance to exit Act 47 oversight successfully, it must align its growth in workforce expenditures with the growth in the revenues available to pay for them.

The following table shows the City's historical personnel costs and the tax revenues available to pay for them. Even with headcount reductions and measures to control the growth in health benefits, the City's personnel costs still grew at annual rate of 1.2 percent. The City's tax revenues, on the other hand, dropped by 0.2 percent annually even when the City's tax rate increased by 17.1 percent from 2013 to 2017.

Personnel Cost and Tax Revenues, 2013 - 2017

	2013	2014	2015	2016	2017	2013-17
Cash compensation	6,921,323	7,154,914	7,219,669	6,973,744	6,933,886	0.0%
Net health benefits	2,059,652	2,176,574	2,202,074	1,814,283	1,732,231	-3.4%
Pension contributions	1,986,457	2,354,001	3,005,567	2,998,155	3,013,273	8.7%
Employee insurance	381,649	423,955	415,445	352,076	382,099	0.0%
Personnel costs	**11,349,082**	**12,109,444**	**12,842,755**	**12,138,257**	**12,061,489**	**1.2%**
Tax Revenues	**14,664,277**	**14,100,166**	**14,188,868**	**14,777,100**	**14,524,093**	**-0.2%**
Real Estate Tax Rate	11.726	11.726	11.726	12.726	13.726	3.2%

As described in the previous chapters, the City's deficit is projected to increase from $1.1 million in 2020 to $3.2 million 2024 even if it only provides annual wage increases of two percent. For the City to be able to afford wage increases beyond the two-percent assumption in the baseline forecast, the City must find either additional recurring revenues or savings to fund those increases. If the City is able to identify the recurring revenues or savings needed to pay for desired wage increases, the Coordinator will review those alternatives for discussion and potential incorporation in the exit plan.

Capital and debt management

Pursuant to the recommendation in the 2015 Amended Recovery Plan[29], a stormwater fee was established in 2018 that is estimated to provide $825,000 in annual revenues to maintain the stormwater system and for any emergency repairs required as a result of flooding incidents. As a result of establishing the stormwater fee, the City was able to shift over $100,000 in annual expenditures out of the General Fund, not to mention the practical benefits of having a funding source that is solely dedicated to the maintenance and upkeep of one of the largest City-owned assets.

According to guidance from DCED, the City will be able to keep its Act 47 EIT and gradually shift it toward capital uses through 2022. While this addresses the City's short-term capital needs, the City must find alternative sources of revenue that are recurring and sustainable so that it continues to fund capital projects even after it leaves oversight and loses its taxing authority provided by Act 47. Because the City's ability to issue new debt is limited given the large projected annual deficits, the baseline projection currently assumes no capital funding beyond 2023 and no new General Obligation debt through 2024.

Act 47 Capital EIT, 2019 - 2023

	2019	2020	2021	2022	2023	2024
Act 47 capital EIT rate (residents)	0.20%	0.30%	0.40%	0.45%	0.0%	0.0%
Act 47 capital EIT rate (commuters)	0.15%	0.20%	0.30%	0.35%	0.0%	0.0%
Estimated revenues	**$817,745**	**$1,242,477**	**$1,779,533**	**$2,170,003**	**$679,968**	**$0**

[29] See CP02 on p. 40 of the 2015 Amended Recovery Plan.

Cost recovery

In the 2015 Amended Recovery Plan, the Coordinator identified two primary areas where the City needs to fully recover the cost of providing the service: golf course operations and refuse collection.

Sylvan Heights Golf Course

The 2015 Amended Recovery Plan recommended that the City recover its full cost of operating the golf course by partnering with an external private entity to eliminate the operating deficits.[30] As of 2019, the City has maintained ownership and operations of the golf course. Even though revenues increased in 2016 and 2017 and helped the City reduce the operating deficits in those years, the golf course is still operating at a loss once capital expenditures are included.

Revenues and Expenditures of the Sylvan Heights Golf course, 2013 -2017

	2013	2014	2015	2016	2017
Revenues	212,328	211,895	238,000	258,295	256,033
Expenditures	229,232	237,619	258,149	228,165	256,366
Net operating result	**($16,904)**	**($25,724)**	**($20,149)**	**$30,129**	**($333)**
Capital expenditures	62,650	54,240	64,000	116,277	0
Net result incl. capital	**($79,554)**	**($79,964)**	**($84,149)**	**($86,148)**	**($333)**

From 2013 to 2017, the City spent almost $300,000 on capital improvements at the golf course, which is more than one year's worth of revenues generated by the golf course. This is also equivalent to 7.8 percent of the City's total capital spending during the same five-year period, even though golf course operations represent one percent of the City's 2019 operating budget. In other words, the City is allocating a disproportionately large amount of capital funding toward the Sylvan Heights Golf Course. Every dollar that the City spends at the golf course is a dollar that it cannot spend on street paving, bridge and building maintenance, Cascade Park, vehicle placement, or other priorities. Given the City's deadline to exit Act 47 oversight and other competing spending needs, the City must find a way to eliminate the operating deficits.

Sylvan Heights Golf Course Capital Projects, 2013 – 2017

Cart replacement	156,175
Dredge and treat lakes	31,739
Vehicle replacement	31,343
Roof repairs	30,911
Pave cart paths	25,000
Clubhouse renovation	22,000
Total	**$297,167**

Refuse Collection

The 2015 Amended Recovery Plan highlighted the City's need to maintain cost recovery in its refuse collection program, and recommended that the City adjust its fees to eliminate the projected deficits. Pursuant to the Coordinator's recommendation, the City increased its blue bag fees in 2016 from $2.0 to $2.2 per bag. Revenues increased as a result of the fee increase, though not as much as anticipated because residents bought fewer blue bags when the City increased the fee.

Refuse Collection Fee, 2013 - 2017

	2013	2014	2015	2016	2017	2015 -17
Refuse collection fee	$803,542	$786,435	$772,362	$829,612	$816,359	**5.7%**
Blue bag fee	$2.00	$2.00	$2.00	$2.20	$2.20	**10.0%**
Est. # of bags sold	401,771	393,218	386,181	377,096	371,072	**-3.9%**

[30] See initiative SH01 on p. 117 of the 2015 Amended Recovery Plan.

While the declining number of occupied housing units may be one of the reasons for the reduced number of bags sold, the more likely reason is that residents are using fewer bags as a result of the fee increase. The City reported increased illegal dumping as residents disposed trash in public trash cans, hillsides, sidewalks, and commercial trash cans to avoid having to buy and use the blue bags. The City also saw an increase in the amount of solid waste mixed into recycling materials. As a result, the City introduced a $0.50 monthly charge for residential property owners to recover the penalty charges. The monthly charge increased to $0.70 in 2018.

The City explored contracting trash collection out to a private entity and issued a request for bids in 2018. The Coordinator reviewed the proposals and concluded that if the City was able to transition its four full-time refuse collection employees to the potential contractor, contracting out trash collection would help the City reduce the operating deficits and provide residents with a higher level of services, including bulk trash collection and more frequent recycling collections. Moving from the current pay-as-you-throw model (where users are charged based on the amount of waste they present for collection) to a fixed fee model (where residents are levied the same fee regardless of the amount of waste) may also help reduce the amount of illegal dumping in the City.

Even though contracting out trash collection would bring a number of financial, operational, and quality-of-life benefits, the City ultimately decided to keep trash collection as an in-house operation. This decision was based, in part, on some residents – mostly one-person households and small families – likely having to pay a higher price for trash collection if the City contracted its services out. The City was also reluctant to eliminate its four refuse collection positions.

Moving forward, the City proposes to move from the current pay-as-you-throw program to a fixed fee program while maintaining the operations in-house. The City also proposes to provide bulk trash pickup to reduce the problem of littering and illegal dumping. The Coordinator will review the City's proposal as part of the exit plan process and will recommend the course of action to help the City eliminate operating deficits and improve the quality of life in the City.

Conclusion

Even though the City has made progress since entering Act 47, there is much more to be done in order for the City to successfully exit oversight. At the most basic level, the City must find ways to structurally balance its expenditures against revenues so that it can continue to fund basic municipal services even after the City loses the additional taxing authority provided by Act 47. Similar to many other Pennsylvania local governments, the City must also control its personnel cost growth given the City's relatively flat tax base and strategically advance its economic development and capital improvement efforts in order to stabilize its tax base and attract residents, businesses, and visitors.

While this Report articulates current financial conditions and ongoing challenges that the City must tackle for the next three years as it prepares to exit oversight, the three-year exit plan will provide strategies designed to provide New Castle a better chance of successfully exiting oversight at the end of 2022.

Appendix

Baseline Revenue Projections

	2019 Budget	2020 Projected	2021 Projected	2022 Projected	2023 Projected	2024 Projected
Real Estate Tax	6,708,605	6,685,003	6,664,398	6,631,467	6,598,974	6,566,645
Earned Income Tax	7,003,297	7,117,314	7,233,351	7,351,445	5,863,848	5,066,005
Local Services Tax	430,000	430,000	430,000	430,000	430,000	430,000
Business Privilege Tax	451,769	400,074	400,074	400,074	400,074	400,074
Mercantile Tax	269,222	192,340	192,340	192,340	192,340	192,340
Deed Transfer Tax	115,000	115,000	115,000	115,000	115,000	115,000
Other Taxes	116,153	106,153	96,153	86,153	76,153	66,153
Total Local Taxes	**$15,094,046**	**$15,045,883**	**$15,131,315**	**$15,206,478**	**$13,676,389**	**$12,836,216**
General Licenses and Permits	523,953	373,351	380,818	388,434	396,203	404,127
CATV Permits	315,000	318,150	321,332	324,545	327,790	331,068
Fines	71,000	72,562	74,158	75,790	77,457	79,161
Total Licenses, Permits and Fines	**$909,953**	**$764,063**	**$776,308**	**$788,769**	**$801,450**	**$814,356**
Sale of Property	100	100	100	100	100	100
Rentals	14,400	14,717	15,041	15,371	15,710	16,055
Total Sales and Rentals	**$14,500**	**$14,817**	**$15,141**	**$15,471**	**$15,810**	**$16,155**
General Grants and Gifts	93,899	93,899	93,899	93,899	93,899	93,899
State Pension Aid	741,600	767,556	794,420	822,225	851,003	880,788
Transfer from Liquid Fuels	335,000	335,000	335,000	335,000	335,000	335,000
Transfer from CDBG	150,000	150,000	150,000	150,000	150,000	150,000
Total Federal, State and County Grants and Loans	**$1,320,499**	**$1,346,455**	**$1,373,319**	**$1,401,124**	**$1,429,902**	**$1,459,687**
Refuse Collection Fee	797,000	815,000	815,000	815,000	815,000	815,000
Water Bill Fee	168,000	171,696	175,473	179,334	183,279	187,311
Code Departmental and Rental Fees	184,250	184,250	184,250	184,250	184,250	184,250
Golf Course Revenue	255,500	260,610	265,822	271,139	276,561	282,093
Employee Hospitalization Contribution	113,685	223,307	249,408	278,175	309,873	345,276
School District Collection Fee	122,500	122,500	122,500	122,500	122,500	122,500
Other	463,322	469,186	475,179	481,304	487,563	493,961
Total Departmental Earnings	**$2,104,257**	**$2,246,549**	**$2,287,632**	**$2,331,701**	**$2,379,026**	**$2,430,390**
Transfer from Marcellus Shale gas	0	0	0	0	0	0
Transfer from Parking	100,000	100,000	100,000	100,000	100,000	100,000
Total Transfers	**$100,000**	**$100,000**	**$100,000**	**$100,000**	**$100,000**	**$100,000**
TOTAL REVENUES	**$19,543,254**	**$19,517,766**	**$19,683,715**	**$19,843,544**	**$18,402,577**	**$17,656,805**

Baseline Expenditure Projections by Category

	2019 Budget	2020 Projected	2021 Projected	2022 Projected	2023 Projected	2024 Projected
Salaries and Longevity	6,363,012	6,516,457	6,675,285	6,823,330	6,978,338	7,124,633
Other Cash Compensation	437,963	456,496	465,511	472,354	479,695	486,611
Overtime	441,084	459,879	478,853	496,314	511,410	530,361
Active Employee' Benefits	1,520,297	1,679,078	1,767,797	1,861,958	1,961,648	2,067,642
Retirees' Benefits	351,832	395,681	422,723	451,639	482,559	515,622
Workers' Comp and Unemployment	420,276	442,383	450,905	459,597	468,464	477,508
Pension Contribution	2,995,783	3,032,147	2,937,292	2,928,643	3,021,839	2,934,263
Workforce Expenditures	**$12,530,247**	**$12,982,121**	**$13,198,366**	**$13,493,835**	**$13,903,951**	**$14,136,640**
General Contracted Services	888,687	912,196	936,472	961,542	987,439	1,014,193
Engineering Services	75,000	76,650	78,336	80,060	81,821	83,621
Sanitary Landfill	180,000	189,000	198,450	208,373	218,791	229,731
Multiperil Insurance & Pension Administration	475,000	497,381	511,280	525,574	540,274	555,391
Contractual Services	**$1,618,687**	**$1,675,227**	**$1,724,538**	**$1,775,548**	**$1,828,325**	**$1,882,936**
Utilities	962,600	994,946	1,021,539	1,048,865	1,076,947	1,105,806
Vehicle Repairs	175,000	183,750	192,938	202,584	212,714	223,349
Other Materials and Supplies	461,570	471,724	482,102	492,708	503,548	514,626
Materials and Supplies	**$1,599,170**	**$1,650,420**	**$1,696,578**	**$1,744,158**	**$1,793,209**	**$1,843,782**
Capital Expenditures	**$817,745**	**$1,242,477**	**$1,779,533**	**$2,170,003**	**$679,968**	**$0**
Debt Service	**$2,962,337**	**$2,941,899**	**$2,953,173**	**$2,966,986**	**$2,972,764**	**$2,955,894**
Transfer to Reserve	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**
Other Expenses	**$83,347**	**$83,144**	**$82,948**	**$82,758**	**$82,577**	**$82,402**
TOTAL EXPENDITURES	**$19,611,533**	**$20,575,288**	**$21,435,137**	**$22,233,288**	**$21,260,793**	**$20,901,653**

Baseline Expenditure Projections (by Department)

	2019 Budget	2020 Projected	2021 Projected	2022 Projected	2023 Projected	2024 Projected
Council	152,041	157,476	159,798	162,192	164,643	167,167
Controller	32,872	31,638	32,652	33,736	34,895	36,133
Mayor	108,552	109,560	110,585	111,630	112,698	113,787
Solicitor	232,205	240,304	246,105	252,118	258,336	264,784
Elected and Executive Officials	**$525,670**	**$538,978**	**$549,139**	**$559,677**	**$570,572**	**$581,871**
Administration	273,970	279,908	286,901	294,136	301,580	309,278
Treasurer	190,023	192,332	197,418	202,695	208,126	213,753
Parking	49,429	54,252	55,557	56,913	58,322	59,787
Central Services	882,195	914,685	938,950	963,872	989,469	1,015,761
Employee Benefits	418,500	440,897	449,715	458,709	467,883	477,241
Financial Management	**$1,814,117**	**$1,882,074**	**$1,928,540**	**$1,976,325**	**$2,025,380**	**$2,075,819**
Engineering Contractual	75,000	76,650	78,336	80,060	81,821	83,621
Streets and Bridges	542,301	541,845	557,762	574,365	591,550	609,494
Sewer	7,000	7,154	7,311	7,472	7,637	7,805
Capital	817,745	1,242,477	1,779,533	2,170,003	679,968	0
Infrastructure Costs	**$1,442,046**	**$1,868,126**	**$2,422,943**	**$2,831,900**	**$1,360,975**	**$700,920**
Building Custodian	118,392	120,640	123,409	126,251	129,155	132,138
Refuse Collection	584,035	600,315	619,862	640,123	661,203	683,215
Public Works Administration	401,449	407,807	418,700	430,006	441,704	453,855
Street Lighting	335,000	343,375	351,959	360,758	369,777	379,022
Municipal Garage	332,230	345,794	359,822	374,521	389,885	405,990
Electricians	116,749	119,022	122,028	125,140	128,333	131,641
Parks and Recreation	234,503	242,016	249,406	257,159	265,244	273,735
Park Maintenance	20,000	20,440	20,890	21,349	21,819	22,299
Maintenance Costs	**$2,142,359**	**$2,199,408**	**$2,266,076**	**$2,335,308**	**$2,407,121**	**$2,481,895**

	2019 Budget	2020 Projected	2021 Projected	2022 Projected	2023 Projected	2024 Projected
Golf	197,162	200,601	203,952	207,435	211,057	214,823
City Subvention Transit	182,010	191,111	200,666	210,699	221,234	232,296
Library Fund, Booster Club and Over 30 Dances	77,647	77,273	76,900	76,530	76,161	75,794
Pension Administrative Costs	125,000	127,750	130,561	133,433	136,368	139,368
Other Professional Services	**$581,819**	**$596,734**	**$612,079**	**$628,097**	**$644,820**	**$662,282**
Police	3,834,310	4,046,623	4,179,385	4,318,112	4,458,965	4,596,551
Fire	2,472,554	2,570,523	2,666,245	2,745,649	2,832,602	2,922,319
Crossing Guards	37,985	37,990	37,994	37,999	38,003	38,008
Public Safety	**$6,344,849**	**$6,655,136**	**$6,883,624**	**$7,101,759**	**$7,329,570**	**$7,556,877**
Code Enforcement	612,650	664,840	682,367	700,606	719,543	739,259
Planning and Zoning	85,203	88,259	90,682	93,203	95,829	98,564
Health Department	26,029	27,510	27,510	27,510	27,510	27,510
Community and Economic Development	78,670	80,177	81,710	83,274	84,869	86,497
Community and Economic Development	**$802,552**	**$860,786**	**$882,269**	**$904,593**	**$927,752**	**$951,831**
Pension Contribution	**$2,995,783**	**$3,032,147**	**$2,937,292**	**$2,928,643**	**$3,021,839**	**$2,934,263**
Debt Service	**$2,962,337**	**$2,941,899**	**$2,953,173**	**$2,966,986**	**$2,972,764**	**$2,955,894**
TOTAL EXPENDITURES	**$19,611,533**	**$20,575,288**	**$21,435,137**	**$22,233,288**	**$21,260,793**	**$20,901,653**

Summary Projections (Rounded)

	2019 Budget	2020 Projected	2021 Projected	2022 Projected	2023 Projected	2024 Projected
Total Revenues	19,543,000	19,518,000	19,684,000	19,844,000	18,403,000	17,657,000
Total Expenditures	19,612,000	20,575,000	21,435,000	22,233,000	21,261,000	20,902,000
Annual Surplus/Deficit	***($69,000)***	***($1,057,000)***	***($1,751,000)***	***($2,389,000)***	***($2,858,000)***	***($3,245,000)***
FY Ending Fund Balance	***$4,804,000***	***$3,746,000***	***$1,995,000***	***($395,000)***	***($3,253,000)***	***($6,498,000)***