

REFERENCE MANUAL NO. 7



Taxation and State Finance



THE PENNSYLVANIA
CONSTITUTIONAL CONVENTION — 1967—

The Preparatory Committee for the Constitutional Convention has prepared a series of nine Reference Manuals for the information of the delegates to the Convention. They are intended to give delegates general information on the Convention, to present a brief history of the several constitutions of Pennsylvania, and to provide pertinent information concerning each of the subject areas that the Convention is authorized to consider. The nine Manuals are—

- No. 1 The Convention
- No. 2 Constitutions of Pennsylvania—
Constitution of the United States
- No. 3 A History of Pennsylvania Constitutions
- No. 4 Local Government
- No. 5 The Judiciary
- No. 6 Legislative Apportionment
- No. 7 Taxation and State Finance
- No. 8 Bibliography
- No. 9 Index

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TAXATION AND STATE FINANCE

The Pennsylvania Constitutional Convention
1967-1968

Taxation and State Finance

REFERENCE MANUAL NO. 7



Prepared for the Delegates by
THE PREPARATORY COMMITTEE
Raymond J. Broderick, Lieutenant Governor, *Chairman*

Commonwealth of Pennsylvania
CONSTITUTIONAL CONVENTION
1967-1968

* * *
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Foreword

Act Number 2, adopted in March, 1967 and ratified by Pennsylvania's voters the following May, authorizes the convening of a Constitutional Convention on December 1, 1967, for a period of three months.

The Act also provides for a Preparatory Committee, to be composed of the Lieutenant Governor and twelve officers of the General Assembly, listed opposite. The Act further stipulates that: "The Committee shall initiate any studies, inquiries, surveys or analyses it may deem relevant through its own personnel or in cooperation with any public or private agencies, including institutes, universities, foundations or research organizations."

Responding to this assignment, the Preparatory Committee appointed a staff under the direction of John W. Ingram, to plan and coordinate its studies. It also appointed four Directors, each commissioned to direct studies in one of the four subject areas within the jurisdiction of the Convention.

In commissioning the studies, the Preparatory Committee directed the staff to trace the historical development of each subject; to analyze judicial interpretations, experience in other states, and national trends; to identify the issues and to compile alternative proposals for constitutional changes to be considered by the Convention. Specific instructions were given the directors to refrain from making any evaluation of alternative proposals cited in the studies, it being the intent of the Preparatory Committee that such evaluations are the proper function of the Convention.

Results of the studies in each area are presented in a series of Reference Manuals, specifically intended to serve as reference sources to which the delegates might turn during their deliberations for information on the many and complex questions which may come before the Convention.

To serve as Directors of its studies, the Preparatory Committee was fortunate to obtain four eminently qualified and prominent authorities. One of these is David H. Kurtzman, at the time Chancellor Emeritus of the University of Pittsburgh and now Pennsylvania's Superintendent of Public Instruc-

tion. Dr. Kurtzman directed the research for and preparation of this Manual on Taxation and State Finance.

For Dr. Kurtzman's personal contribution of time and capabilities in the carrying out of this assignment, the Committee is deeply appreciative. Special commendation is due him in view of the extremely difficult time schedule allowed to complete this Manual. It is also appropriate to acknowledge the cooperation of the University of Pittsburgh for making Dr. Kurtzman available for this assignment.

The Preparatory Committee is pleased to submit this Reference Manual to the Convention delegates, for whose assistance it is intended.

Raymond J. Broderick

Chairman

Preface

This volume deals with those sections of Article IX affecting State Taxation and Indebtedness. The section on Local Government Debt is included in the volume on Local Government.

The chapter dealing with Budgeting is not now covered in Article IX of the Constitution. This subject, indeed, is not treated as such in the present Pennsylvania State Constitution, although some portions of it are covered in the articles dealing with State Legislation and the Executive. It is included here for the purpose of calling to the attention of the Constitutional Convention that it might find desirable to include such a section should it amend section 4 of Article IX.

Throughout the report there are no specific recommendations made on any of the subjects but rather series of alternatives are listed for the consideration of the delegates to the Convention.

The Director wishes to acknowledge the help rendered by the staff working on this volume which include Mr. Neil C. Blanton, Mr. R. Stanton Wetick, Jr., Dr. Rosalind Branning, Mrs. Margaret Gold and Mr. Fred Frank.

Special thanks are due to the Pennsylvania Economy League, Western Division, for making available to the Preparatory Committee the services of Mr. Neil C. Blanton, without any cost to the Committee.

The Director hopes that the delegates to the Convention will find this material helpful in their deliberations.

David H. Kurtzman
Director
Taxation and State Finance

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Introduction

The material in this booklet deals with the applicable sections of Article IX of the Constitution concerning *Taxation and Finance*.

The Act¹* establishing this Convention specifically prohibits consideration or change of the "uniformity clause" in Section 1 and Section 18 earmarking gasoline taxes for the Motor License Fund. The remaining 23 sections deal with four general subject areas: tax exemption, State debt, municipal debt, and the handling of State funds.

The text of Article IX is presently the longest in the Constitution and it has been the most amended Article. Ten amendments have been added to permit specific borrowing by the State since the \$1 million limit was imposed.

The sections governing the incurrence of municipal debt have been modified seven times, with five of the amendments relating to Philadelphia alone.

Every major attempt to modernize the Constitution has proposed substantial change in this Article.

HISTORY

The interpretation of law is often influenced by the "intent" of writers. Thus, the events of their times and the subsequent effect upon the thinking of the delegates to the Convention of 1873 may be of interest to the delegates of this Convention.

The framers of the first three Pennsylvania Constitutions 1776, 1790, 1838 were not preoccupied with problems of taxation, finance, or debt. Indeed, the subject was hardly mentioned except as to the treatment of individual debtors and the payment of taxes by electors. The Legislature was left with complete discretion in this area.

Given this unlimited authority the Legislature, with general public support, launched in 1826 an ambitious program of public works—the principal item of which was the Pennsylvania Main Line project to connect Pittsburgh and Philadelphia by a system of canals and railways. At the be-

*Footnotes will be found at the end of each chapter.

ginning of this project, State debt stood at \$2,500,000. By 1847, State debt had risen to \$36,000,000 and the canal system was losing more than \$1 million a year. In 1839, Pennsylvania defaulted both principal and interest and in 1841, borrowed \$870,000 to make interest payments alone. In 1857-58 the public works were sold for \$11,000,000 and a disillusioned public amended the Constitution to place the present restrictions on State debt.

The Civil War took attention from the financial scene but the post-war years were the most corrupt in the history of the State. An uninhibited Legislature granted special favors in wholesale quantities. Law making at that time became a scramble to bestow special privileges upon favored interests and constituents, who in turn amply rewarded the members of the Legislature. As an illustration, during the 1867-73 period the Legislature passed 8,755 private acts and only 475 general laws.

Municipalities faced with an era of unprecedented population growth and industrial development vied with each other for access to markets and facilities to serve their growing population. For example, Pittsburgh borrowed \$1,700,000 to invest in railroad stocks. Of the \$50,000,000 outstanding in County debt, \$44,000,000 was for Philadelphia alone so it was not surprising that the Philadelphia delegates were most active in pressing for a limit on municipal borrowing.

This kind of activity was not peculiar to Pennsylvania at this time. Eighteen other states had imposed comparable debt restrictions on their Legislatures by the time Pennsylvania amended its Constitution in 1857. The Tweed ring in New York was being exposed in 1873 as the Convention was in session.

In this setting, the Convention reaffirmed the restrictions on State debt established in 1857 and added constitutional restrictions on municipal borrowing.

MAJOR STATUTORY AND JUDICIAL DEVELOPMENTS

The effect of strict constitutional limits was to severely restrict governmental borrowing for 75 years. Then, as is the case with many overly strict limitations, a way was found to by-pass the restrictions. Faced with a lack of borrowing capacity to match federal grants-in-aid during the depression years of the middle 1930's, the State devised a means of evading the constitutional limits by borrowing through an authority. The authority finances its projects by issuing bonds which are repayable either from the revenues of the project if it is self-sustaining, or from rentals from a lease to the governing body if it is not self-sustaining.

The Legislature passed² and the courts approved³ a General State Authority, and a Municipal Authorities Act followed. World War II brought a halt to capital programs and the G.S.A. was liquidated in 1945.

However, by 1949, the pent-up demand for capital improvements brought about the restoration of the G.S.A. and the passage of a strength-

ened Municipal Authority Law.⁴ Most of the capital improvements in the past 20 years have been financed by this method. Ninety percent of present State debt outstanding and two-thirds of local borrowing is presently done through an authority. Between 1945 and 1965, 1,690 municipal authorities were formed to borrow \$3.3 billion dollars.

MAJOR ISSUES AND OBJECTIVES

"Ideally, a constitution should be silent on the subject of taxation and finance, thus permitting the Legislature and the Governor freedom to develop fiscal policies for the State to meet the requirements of their time."⁵

It is obvious that there is room for many degrees and shades of opinion between this statement and the present Pennsylvania Constitutional provisions.

There are several areas of general agreement among the groups testifying before this committee which may be summarized as follows:

Concerning State debt, there was general agreement that it should be liberalized and proposals varied only as to the degree of that liberalization and how it could best be accomplished. These proposals included: that debt be incurred only "for a public purpose," that the purpose "be specified in the statute," that procedural restrictions be included, such as a two-thirds or three-fourths vote of the Legislature, that the debt incurred be limited to "the useful life of the project," that the statute authorizing debt "contain the means to pay principal and interest," that debt in any amount be incurred when approved by the electorate, that borrowing in the State's own name be as liberal as that permitted by the G.S.A., that borrowing be unlimited for capital improvements. There is some opinion that any liberalization not granting some capacity as "usable" as the authority method would not change the situation.

In any event there seems to be little sentiment, among those testifying, that the provision be left "as it is."

On the question of tax exemption there is a recommendation to leave the present constitutional provision for tax exemptions intact. This position is contrasted with a strong proposal to abolish all exemptions. It should be kept in mind that with one exception, these exemptions are not mandatory and are all affected by legislative enactment and many of the problems in this area lie in the legislation putting the exemption into effect and the subsequent interpretations of these laws by the Courts.

The compelling reason for calling the Constitutional Convention of 1873 was to correct legislative abuse. The principal reason for the convening of the Convention of 1967 is to modernize some of the outdated rigid provisions of the 1874 document.

In the calling of the Convention, the Legislature recognized that modernizing of the debt provisions were needed; that, in fact, the long and

uncertain path of constitutional amendment does not provide the speed and flexibility which the State and its municipalities need to provide the facilities which its citizens demand.

Notes to Introduction

1. Act 2 of March 15, 1967.
2. Act of June 28, 1935 (P.L. 452).
3. Kelly vs. Earle, 325 Pa. 337 (1937).
4. P. L. 382 of 1945.
5. Kresky, Edw. M. —*Salient Issues of Constitutional Revision*; National Municipal League—1961, pp. 136.

CHAPTER 1

Tax Exemptions

SCOPE OF THE PROBLEM

The power to tax is an inherent power of the State vested absolutely in the Legislature and hence is exercisable even in the absence of specific authorization in the Pennsylvania Constitution. Except as limited by the State and Federal Constitutions and the laws of the United States, the power to tax is bounded only by the necessity of the State.¹

The major limitation imposed upon the State's power of taxation by the State Constitution is the uniformity clause contained in Section 1 of Article IX which reads as follows:

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

This Constitutional Convention is prohibited from considering or including in its recommendations any proposal which would modify, alter, or change in any respect the above portion of the Constitution by the Act of the General Assembly providing for the Constitutional Convention.²

The remainder of Section 1, together with Section 1B of Article IX, makes provision for certain exceptions to the uniformity clause. Section 1, as originally adopted, authorized the Legislature to exempt from taxation public property used for public purposes, places of worship, certain places of burial and charitable institutions. An amendment to the Section adopted in 1923 added property of veterans' organizations to the list of categories which the Legislature could exempt from taxation and another amendment adopted in 1958 authorized the Legislature to make special provisions for the taxation of private forest reserves. These provisions read as follows:

The General Assembly may, by general laws, exempt from taxation public property used for public purposes, actual places of religious worship, places of burial not used or held for private or corporate profit, institutions of purely public charity and real and personal property owned, occupied, and used by any branch, post, or camp

of honorably discharged soldiers, sailors, and marines; and the General Assembly may, by general laws, set up standards and qualifications for private forest reserves, and make special provision for the taxation thereof.

In addition, the following amendment to Section 1, which was adopted in 1965, authorizes any taxing authority to exempt from the occupational privilege taxes any person earning less than \$1,000.

Any taxing authority may exempt from occupational privilege taxes, persons deriving less than \$1,000 per year from such occupation.

Also Section 1B, which was added to the Constitution in 1928, permits exemptions to be granted to residents of other states which grant similar exemptions to Pennsylvania residents. This Section reads as follows:

Taxation laws may grant exemptions or rebates to residents, or estates of residents, of other states which grant similar exemptions or rebates to residents, or estates of residents, of Pennsylvania.

None of the above provisions grants any exemptions. They merely permit the Legislature or other taxing authorities to do so at their discretion.

A 1961 amendment to Section 1, on the other hand, specifically exempts from real estate taxes property of certain disabled veterans.

Citizens and residents of this Commonwealth, who served in any war or armed conflict in which the United States was engaged and were honorably discharged or released under honorable circumstances from active service, shall be exempt from the payment of all real property taxes upon the residence occupied by the said citizens and residents of this Commonwealth imposed by the Commonwealth of Pennsylvania or any of its political subdivisions if, as a result of military service, they are blind, paraplegic, or double or quadruple amputees and if the State Veterans' Commission determines that such persons are in need of the tax exemptions granted herein.

This provision exempting property of certain disabled veterans from real property taxation differs from the others. It is a mandatory grant of exemption while the other provisions merely permit the Legislature at its discretion to provide for the exemption.

The Legislature is restricted to granting exemptions only to the above enumerated categories of property by the uniformity clause and Section 2 of Article IX which provides that

"all laws exempting property from taxation, other than the property above enumerated shall be void."

In addition, the Legislature's power to exclude corporate property from taxation is specifically restricted by Section 3 of Article IX which provides that:

The power to tax corporations and corporate property shall not be surrendered or suspended by any contract or grant to which the State shall be a party.

While the constitutional power to exempt the categories specified above from taxation is merely permissible with the exception of the exemption covering disabled veterans, the Legislature has elected to grant exemptions in all such categories. The impact of such exemptions has been felt primarily in the area of local real estate taxes. In the last definitive statewide study of the property tax exemption in 1957, property assessed at \$2.9 billion and constituting 19 percent of the total assessed valuation of all property within the State was exempt from real estate taxation and in 72 communities property constituting 50 percent or more of the community's total assessed valuation was exempt from real estate taxation.³

Furthermore, in the last ten years the percentage of tax exempt property in the State's two major metropolitan areas has substantially increased. More than \$768 million (a 47 percent increase) of exempt property has been added to the tax rolls of Philadelphia and Allegheny County in this period. See Table 1 on next page. As a result, there has been an increase in the percentage of exempt property from 20 percent to 24.3 percent in Philadelphia and from 26 percent to 32.4 percent in Pittsburgh.

In addition to the real estate exemptions, the Legislature has also granted exemptions to these groups mentioned in the Constitution from non-property taxes such as the sales and use tax, mercantile tax and business receipts tax.

At the time of this writing 21 bills proposing new exemptions have already been introduced in the 1967 Session of the Legislature. Thirteen of them propose amendments to Section 1 of the Constitution extending the exemption from property, sales and other taxes to individuals because of age, physical infirmity, or limited income.

Two of the seven groups testifying before the Preparatory Committee on this Section proposed a thorough tightening of these exemptions and the Local Government Conference group proposed eliminating all exemptions.

HISTORY

Before the adoption of the 1874 Constitution there was no limitation on the power of the Legislature to grant exemptions from taxation either by general laws or special laws. Section 1 was enacted to eliminate the power of the Legislature to grant exemptions capriciously and to limit the granting of exemptions to certain specified categories. The amendments to Section 1, beginning in 1923 with the exemption for property of veterans' organizations, and the addition of Section 1B to the Constitution in 1928 were, of course, to include additional categories for which tax exemptions were permitted.

Section 2 was part of the original 1874 Constitution. Its necessity had been challenged by certain delegates to the 1873 convention. Since Section 1 would require all taxes to be uniform, it was argued that any laws granting

TABLE 1. TAX-EXEMPT REALTY BY CATEGORY, 1966
PHILADELPHIA AND ALLEGHENY COUNTY

	Valuation (Millions)		Percentage of Total Tax-Exempt Valuations	
	Philadelphia	Allegheny County	Philadelphia	Allegheny County
<i>Government Property</i>				
Federal	\$204.1	\$ 17.7	14.5%	1.8%
State	63.3	191.9 ¹	4.5	19.2
City	364.9		26.0	
School District	170.4	280.4 ²	12.1	28.0
Housing Authority	75.0	60.0	5.3	6.0
Redevelopment Authority	37.6	35.8	2.7	3.6
Miscellaneous Authorities	17.2	13.0	1.2	1.3
Subtotal	\$ 932.5	\$ 598.8	66.3%	59.9%
<i>Nongovernment Property</i>				
Churches	\$ 136.5	\$ 107.1	9.7%	10.7%
Cemeteries	8.9	10.5	.6	1.0
Museums, Libraries, Art Galleries	12.8	24.8	.9	2.5
Institutions of Learning	135.6	— ²	9.7	—
Hospitals	92.5	85.6	6.6	8.5
Miscellaneous exempt property	41.2	2.6	2.9	.2
Disabled Veterans	.2	.2	—	—
Veterans' Posts	1.8	2.1	.1	.2
Public Utilities	44.7	170.2	3.2	17.0
Subtotal	\$ 474.2	\$ 403.1	33.7%	40.1%
Grand Total	\$1,406.7	\$1,001.9	100.0%	100.0%

1. No separate breakdown available for state and local government.

2. No separate breakdown available for public and private schools.

Source: Compiled from Allegheny County assessment records and from reports of tax exempt property in Philadelphia, as prepared December 1966 by the Pennsylvania Economy League (Eastern Division).

exemption to groups not enumerated in Section 1 would conflict with Section 1 and necessarily be void. Eventually Section 2 was approved, however, because other delegates believed that it was necessary to repeal existing exemption laws which conflicted with Section 1.

Section 3 was also part of the original 1874 Constitution. Prior to 1874 the Pennsylvania Supreme Court had held unconstitutional a contractual provision exempting from State taxation purchasers of property being sold by the State.⁴ This Section was added to prevent a later court from overruling this decision.

JUDICIAL INTERPRETATIONS

Following the explicit wording of the Constitution, the Pennsylvania appellate courts have ruled in numerous cases that it is beyond the power of

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JUDICIAL INTERPRETATIONS

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stitution's fulfilling its purpose as a place of worship, such as parking lots for use by persons attending religious services and housing facilities for clergy, janitors, etc.¹⁰

On the other hand, the exemptions for public and charitable property, which cover "public property used for public purposes" and institutions of "purely public charity," have been construed by the Pennsylvania appellate courts to include all property convenient and useful to the charitable or public purpose.¹¹ Using this standard, the Pennsylvania appellate courts have upheld exemptions to hospitals for property used as a parking lot for its employees and visitors and property separate from the hospital used as a residence for hospital personnel;¹² to educational institutions for property located off campus and used as a residence for professors and college presidents;¹³ to Young Men's Christian Associations for property used for dormitory, restaurant, coffee shop, barber shop, cafeteria, and bowling alley facilities available to the public;¹⁴ and to Allegheny County for portions of a county-owned-and-operated airport leased to concessionaires for restaurant, coffee shop, parking, and limousine service facilities.¹⁵

Although the provisions in Section 1 permitting exemptions for public, religious and charitable groups refer only to "public property," "actual places of worship," and "institutions of purely public charity," the Legislature has not restricted exemptions for these groups to property taxes. The Legislature has also granted exemptions from such non-property taxes as the sales and use tax, mercantile tax and business receipts tax. The validity of these exemptions has been challenged as unconstitutional in the appellate courts only in the situation in which a charitable organization attempted, without success, to extend the exemption to a commercial enterprise.¹⁶ There are no cases deciding if these exemptions, when applied to the noncommercial activities of these groups, are valid either as an exemption under Section 1 or as an exclusion from taxation of a proper class under the uniformity clause.

TREATMENT IN OTHER STATES

The treatment of tax exemptions in state constitutions can be considered in three main categories: (1) no specification of any kind, leaving the Legislature free under its general powers to grant exemptions and to alter or revoke them at any time; (2) a broad and brief provision setting forth a few specific mandates on the Legislature to grant exemptions or a few specified restrictions on its powers to do so, leaving the Legislature otherwise free to act under its general powers; and (3) a detailed and lengthy regulation enumerating the types of property that may or shall be exempted by the legislature and barring others not enumerated in the constitution. The types of property, persons and organizations for which various state constitutions expressly permit or grant exemptions include, in addition to the types enumerated in the Pennsylvania Constitution, agricultural and horticultural

societies, agricultural fair associations, athletic clubs, auditoriums, disabled persons, electric cooperatives, grape vines, homesteads, literary organizations, manufacturing plants, public utilities, property devoted to scientific purposes, urban redevelopment property, low income housing, parents and unmarried widows of war dead, and persons over sixty-five.

ALTERNATIVE PROPOSALS

Since the uniformity clause will be included in its present form in any revised Constitution, only exemptions provided for by the revised Constitution will be valid. The Constitution may provide for exemptions either by granting the exemption in the Constitution itself; by authorizing the Legislature or other taxing authorities to grant certain enumerated exemptions if it so chooses; or by removing the present restrictions on the Legislature by giving it the power to grant any reasonable exemptions.

1. *No Substantive Changes*

The revisory commissions proposed no substantive changes to the exemption sections. The *Report of the Commission on Constitutional Revision (1959)* recommended that Sections 1, 1B, 2 and 3 of Article IX be kept in their present form and the only change recommended by the *Report of the Governor's (Scranton) Commission on Constitutional Revision (1964)* was a rewording of the portion of Section 1 granting tax exemptions to certain disabled veterans which would permit the determination of need for the exemption to be made by an "appropriate State Agency" rather than "the State Veterans' Commission."

2. *Abolish all Exemptions*

In contrast, the local government groups testifying before the Preparatory Committee called for the abolishment of all real estate exemptions. They proposed that Section 1 of Article IX be amended to read as follows:

"All taxes shall be uniform upon the same class of subjects, within the territorial limit of the authority levying the tax, and shall be levied and collected under general laws; *such general laws shall provide for no tax exemptions on property*, including all property owned or leased by the Commonwealth, its agencies, and its political subdivisions."¹⁷

The reasons generally given for such an approach are that all property must be given municipal services and since the property tax is the principal source of revenue for municipalities all properties should pay equally.

3. *Tighten the Present Exemptions*

Action along the same line, but less drastic, was proposed by other groups testifying before the Preparatory Committee's Sub-committee on

Taxation and Finance.¹⁸ These proposals included the recommendations of the abolishment of the exemption for public utilities and a tightening of the other exemptions.

The difficulty of retaining but tightening the other exemptions was recognized by these groups during their testimony. The court decisions, as was previously discussed, do not permit the exemption of property not used for public, religious or charitable purposes. Hence, to tighten the exemption would require the exclusion from tax exempt status of certain property used in connection with charitable, religious or public purposes.

This raises several problems. The first is deciding where to draw the line. Should the Constitution prohibit exemptions for restaurants in government buildings used primarily by public employees; for non-profit hospitals, which charge for their services; for college dormitory facilities? And even if one is able to decide where the line should be drawn in each situation, what language should be put into the Constitution that will be general enough to deal with many situations and yet specific enough to provide solutions in these difficult areas? These difficulties would support the position that it is more feasible to leave the tightening of exemptions to the Legislature which can pass legislation directed to the particular abuse.

4. Public Utility Exemption

If the continuation of the exemption for property of public utilities is desired, it may be advisable to strengthen the Constitutional basis for this exemption by adding a provision to Section 1 of Article IX authorizing the Legislature to exempt such property. If, on the other hand, the abolishment of the exemption for property of public utilities is desired, consideration should be given to adding to the Constitution (perhaps to Section 2) a clause providing that such property shall not be exempt from taxation.

5. Exemption from Non-Property Taxation

One possible method of eliminating the ambiguity in Section 1 of Article IX concerning the type of taxes for which exemptions may be granted is to re-word the Section to specifically authorize the Legislature to grant exemptions from any and all taxations to religious, charitable, and public bodies for property used for and activities relating to public purposes, religious worship, and charitable purposes.

Notes to Chapter I

1. There are several significant limitations imposed upon the State's taxation power by the Federal Constitution: The Fourteenth Amendment prohibits a state from discriminatorily subjecting persons and property to taxes not imposed on others of the same class; the "commerce clause" limits the power of states to tax certain activities and businesses in-

volving interstate or foreign commerce; and the principle that a sovereign cannot be taxed without its consent shields the property and activities of the Federal Government from state taxation unless Congress has provided to the contrary.

2. Act 2 of March 15, 1967.
3. Tax Exempt Real Property—1957—State Tax Equalization Board.
4. *Mott v. Pennsylvania Railroad Co.* 30 Pa. 9 (1858).
5. See *New Castle v. Lawrence County*. 353 Pa. 175, 183-4 (1945); *Clearfield Bituminous Coal Corp. v. Thomas* 336 Pa. 577-8 (1939); *Board of Christian Education of the Presbyterian Church v. Philadelphia School District* 171 Pa. Super. 610, 615-6 (1952).
6. See Walker, *Exemption of Real Property of Public Utilities from Local Taxation in Pennsylvania*. 13 University of Pittsburgh L. R. 263 (1951-2). But see *Independence Township School District Appeal* 412 Pa. 302, 309 (1963) where the Court classified property of a public utility as "public property used for public purposes."
7. *Tax Exempt Real Property*, State Tax Equalization Board, 1957.
8. See *Jones & Laughlin Tax Assessment Case* 405 Pa. 421, 433-6 (1961).
9. See *West View Borough Municipal Authority Appeal* 381 Pa. 416, 420 (1955); *Board of Christian Education of the Presbyterian Church v. Philadelphia School District* 171 Pa. Super 610, 616 (1952); *Moon Township Appeal* 387 Pa. 144, 149 (1956).
10. *Second Church of Christ Scientist of Philadelphia v. Philadelphia* 398 Pa. 65 (1959).
11. See *Pittsburgh Bible Institute v. Board of Property Assessment, Appeals and Review* 405 Pa. 297, 302-3 (1961); *Lancaster Theological Seminary Tax Exemption Case* 207 Pa. Super 12, 14 (1965).
12. *Shadyside Hospital Appeal* 207 Pa. Super 261 (1966); *Allegheny General Hospital v. Allegheny County Board of Property Assessment, Appeals and Review* 207 Pa. Super 266 (1966).
13. *University of Pittsburgh Tax Exemption Case* 407 Pa. 416 (1962); *Lancaster Theological Seminary Tax Exemption Case* 207 Pa. Super 12 (1965).
14. *Young Men's Christian Association v. Reading* 402 Pa. 592 (1961); *Young Men's Christian Association of Pittsburgh Tax Case* 383 Pa. 176 (1955).
15. *Moon Township Appeal* 387 Pa. 144 (1956).
16. *Board of Christian Education of Presbyterian Church v. Philadelphia School District* 171 Pa. Super 610 (1952).
17. *Local Government Conference*, Annex, p. 74.
18. *Pennsylvania Home Builders Association*, Annex p. 64. *Pennsylvania A.F.L.-C.I.O.*, Annex p. 55.

CHAPTER 2

State Finance

INTRODUCTION

The control of the State's finances is inherently vested in the Legislature whose power is supreme unless limited by the Constitution.

The Pennsylvania Constitution imposes numerous restrictions upon the power of the Legislature to control the State's finances. One of the most significant of these is a prohibition against borrowing except for certain limited purposes. In addition, the Constitution, among other things, prohibits the pledging of the State credit to private bodies; requires all laws authorizing borrowing to specify the purpose for which the borrowed funds are to be used; requires the Legislature to maintain a sinking fund for the payment of State debt; limits the investment of State surplus funds to bonds of the United States and Pennsylvania; and provides certain punishments for the misuse of the State moneys. The principal problem facing the Convention in the area of State finances is that of determining whether or not to give to the Legislature more control over the State's finances by easing or removing any of these restrictions.

BORROWING RESTRICTIONS

Scope of the Problem

Section 4 of Article IX prohibits the legislature from creating any debt by or on behalf of the State except to repel invasion, suppress insurrection, defend the State in war, pay existing debt and supply casual (current) deficiencies in revenues not to exceed one million dollars.

This Section reads as follows:

No debt shall be created by or on behalf of the State, except to supply casual deficiencies of revenue, repel invasions, suppress insurrection, defend the State in war, or to pay existing debt; and the debt created to supply deficiencies in revenue shall never exceed, in the aggregate at any one time, one million dollars: Provided, how-

ever, That the General Assembly, irrespective of any debt, may authorize the State to issue bonds, to the amount of one hundred millions of dollars, for the purpose of improving and rebuilding the highways of the Commonwealth.

In effect, this Section currently imposes a constitutional requirement for a balanced budget. Its provisions do not permit the Legislature to incur any debt for capital improvements. The one million dollar limitation for casual deficiencies which did give the Legislature certain leeway in 1873 when the State's total annual expenditures amounted to about \$7 million has lost all significance for the current annual budgets amounting to more than two billion dollars. The State makes no expenditures for the permissible purposes enumerated in Section 4. The provision authorizing the issuance of bonds of \$100 million for highway improvement is not for continual use and hence no longer serves any function because all the bonds were issued long ago.

While a "pay-as-you-go" philosophy may be sensible in handling current expenditures, long term borrowing to finance the State's urgent needs for capital improvements, such as highways, schools, parks, etc., has been a necessity from the depression days. But borrowing directly by the State for such purposes is permissible only by the State's adoption of a Constitutional amendment permitting such borrowing and this has been found to be a slow and uncertain process.

The process is slow because it takes approximately three years to amend the Constitution in Pennsylvania. The procedure for amending the Constitution requires approval of the amendment by a majority vote in two sessions of the General Assembly followed by ratification by the electorate.¹ In addition, amendments covering the same subject matter cannot be submitted more often than once in five years.²

The process is uncertain because the electorate frequently votes down proposed amendments authorizing the Legislature to incur debt. Of the seventeen amendments to increase the State debt which have been submitted to the electorate in the past one hundred ten years since the Constitutional debt restriction was imposed, only ten were approved and of these only six were for capital improvements. The amendments rejected included proposals to incur debt for highways, forest land, mental hospitals, and the refunding of authority bonds.

Authority Financing

To avoid this slow and uncertain process of amending the Constitution to increase the State debt to finance capital improvements the Legislature, beginning in 1935, turned to "authority financing." First used as a means to provide matching funds for P.W.A. projects and R.F.C. loans, this type of financing was revised in the post-World War II years to provide funds for the huge backlog of capital improvements.

An authority is a separate public corporate agency of the State, created by the Legislature and composed largely of public officials. The purpose of

its creation is for the construction of permanent public works and improvements. To finance these projects, it is vested with the power to borrow money and make contracts, subject to the limitation that it can not pledge the credit of the State. It may acquire real and personal property by purchase, eminent domain or lease and may sell or lease the completed projects.

Authority financing involves issuance by an authority of its bonds to obtain funds for the construction of capital improvements. These bonds are repaid out of the revenues derived from the capital improvement if the improvement is revenue producing, such as a toll road, or if the improvement is non-revenue producing, such as a State office building, out of the rentals derived from a long-term lease of the authority's improvement to the State. In the latter instance, the general revenues of the State are used to pay the authority the rentals due under the lease.

There is no limitation upon the amount that the Legislature may borrow for capital improvements through the authority mechanism. As will be discussed in a subsequent section of this Chapter, the courts have ruled that such financing does not come within the coverage of debt limitation provisions of Section 4.

Authority financing has become a popular device for financing capital improvements of the State. As of June 30, 1967, State general obligation bonds outstanding for capital improvements totaled less than 70 million dollars (see Table 2) while State authority bonds outstanding were in excess of one billion dollars.

This outstanding authority indebtedness was incurred by:

(1) The General State Authority which has outstanding indebtedness of \$870 million and additional authorization of \$509 million already approved by the Legislature.

(2) The State Highway and Bridge Authority which has \$253 million in outstanding indebtedness and additional authorization to spend \$870 million approved by the Legislature.

Rental for the projects of these authorities will be paid from the general revenue of the State.³

While the financing of capital improvements through the use of authorities has eliminated the delay and uncertainty encountered under the Pennsylvania Constitutional prohibitions against borrowing, it has created several new problems.

First, the cost of borrowing is higher when authority financing is used. In a study conducted by David H. Kurtzman, then of the Fels Institute in 1963, it was concluded that:

"It is difficult to ascertain with precision this extra cost. However, several studies of this subject estimate this higher interest cost at a minimum of one-quarter of one percent to in excess of one-half of one percent. Even a one-quarter of one percent extra cost in interest over the average life of the authority bonds amounts to about \$42,000 per every million dollars borrowed. Thus, for \$1,092,734,600 of General

TABLE 2. BONDED INDEBTEDNESS OF STATE AUTHORITIES AND SPECIAL FUNDS IN PENNSYLVANIA, June 30, 1967
(In thousands of dollars)

<i>Name of Authority or Fund</i>		<i>Total Bonds Issued</i>	<i>Bonds Redeemed, Matured, or Retired</i>	<i>Bonds Outstanding</i>	<i>Sinking Fund or Reserves</i>	<i>Net Indebtedness</i>
Total		\$2,742,851	\$703,475	\$2,039,376	\$156,091	\$1,883,285
AUTHORITIES						
General State Authority		1,040,250	169,748	870,502	(1) 34,749	835,753
State Highway and Bridge Authority		305,000	52,074	252,926	112	252,814
State Public School Building Authority		533,476	59,551	473,925	(2) 82,764	391,161
Pennsylvania Turnpike Commission		696,625	364,976	331,649	27,099	304,550
Delaware River Port Authority		167,500	57,126	110,374	(3) 11,367	99,007
COMMONWEALTH SPECIAL FUNDS		\$ 285,000	\$ 98,900	\$ 186,241	\$ 55,806	\$ 130,435
Public Building Construction Fund—Series "K"		50,000	30,000	20,000	—0—	20,000
World War II Veterans' Compensation—Series "N"		65,000	32,500	32,500	695	31,805
Korean Conflict Veterans' Compensation—Series "O"		120,000	36,400	83,600	54,531	29,069
Sinking Fund—unclassified and unclaimed		—0—	—0—	(4) 141	201	(5) 60
Project 70 Land Acquisition—Series "Q"		50,000	—0—	50,000	379	49,621

1. Includes revenue fund, principal and interest fund, operating fund, and bond redemption fund.

2. Includes debt service fund, debt service reserves, bond redemption fund, and revenue fund.

3. Includes bond service fund and reserve fund.

4. Non-Interest bearing debt and matured loans unclaimed.

5. Credit Figure.

Source: Tabulated sheets from Governor's Office of Administration, Budget Bureau.

State Authority borrowing authorized September 1, 1963, the additional interest cost over the life of this indebtedness would be approximately \$44 million. This does not include the State Highway and Bridge Authority borrowing."⁴

Proponents of the authority method of financing assert that this difference in interest rates has narrowed as the public became more familiar with the authority and that issues of authority and general obligation bonds under reasonably comparable conditions will show very little difference in interest costs. Table 3 would support this view. The interest costs of the three principal State authorities and Project 70 general obligation bonds are compared for bonds sold in the early summer of 1965. The difference in cost for these issues is very small.

TABLE 3. COMPARISON OF INTEREST COST BETWEEN
COMMONWEALTH OF PENNSYLVANIA AND CERTAIN OF ITS
AGENCIES AS SHOWN BY RECENT BOND SALES

	<i>Project 70 Bonds</i>	<i>The General State Authority</i>	<i>State Public School Building Authority</i>	<i>Highway and Bridge Authority</i>
Sale Date	7/14	6/16	5/5	5/25
Municipal Bond Index	3.33%	3.34%	3.24%	3.26%
Principal Amount	\$27 Million	\$20.250 Million	\$23.075 Million	\$15 Million
<i>Maturity</i>	<i>Reoffering Prices in Decimals</i>			
1966		2.40%	2.45%	2.35%
1967		2.55	2.55	2.50
1968		2.65	2.65	2.60
1969		2.75	2.75	2.70
1970		2.85	2.80	2.75
1971	2.75%	2.90	2.85	2.80
1972	2.80	2.95	2.90	2.85
1973	2.85	3	2.95	2.85
1974	2.875	3	3	2.90
1975	2.875	3.05	3.05	2.90
1976	2.90	3.05	3.05	2.95
1977	2.90	3.10	3.10	2.95
1978	2.95	3.10	3.10	3
1979	2.95	3.15	3.125	3
1980	3	3.20	3.15	3
1981	3	3.20	3.15	3.05
1982	3	3.25	3.20	3.05
1983	3.05	3.25	3.20	3.10
1984	3.10		3.25	3.10
1985	3.10		3.25	4

Source: Compiled from records of the State Treasurer and the several authorities. Readers will note that, while the cost of authority debt is higher than that of general obligation bonds, differences among the three authorities are minor.

Second, authority financing results in additional financial and administrative hindrances. The Kurtzman study concluded that where authority financing is used, there is considerable amount of duplication involved in the examination of plans and inspection of construction because of the addition of one more agency to the various State agencies already concerned with the planning and execution of capital improvement projects. It also concluded that "Aside from the duplication of costs involved, it can be said that of the additional financing costs through G.S.A. brought about by legal requirements, conditions of bond sales, or administrative practices, about 14 percent would be financed from current revenues (instead of borrowed moneys with the related interest costs of such financing) and a portion of these percentages would not have to be spent at all, if these projects were financed through general obligation bonds."⁵

Third, authority financing has removed all direct control of the electorate over borrowing to finance capital improvements. Because the Courts have ruled that authority financing is outside the coverage of Section 4 of Article IX there is no limitation upon the power of the Legislature to empower authorities to issue bonds. Thus, the Legislature has virtually the same power to finance capital improvements through borrowing as if Section 4 specifically excluded from its prohibition debt created to finance capital improvements. (This, of course, is not viewed as a problem for those who favor the elimination of restrictions upon the Legislature's power to incur debt for public improvements).

Fourth, there are administrative hinderances to the sound planning of capital improvements resulting from the State's use of authority financing. The authorization of funds for capital improvements is made through a separate act which is not considered an appropriation act. The Governor, therefore, cannot exercise his "item veto" power. As a result of this many "pet" projects of individual legislators which were not requested by the Governor in his capital budget are included in the act authorizing funds for capital improvements.

History of Section 4

The Pennsylvania Constitution of 1776, 1790, and 1838 contained no provision for controlling public debt. Indeed, none of the original State Constitutions contained any such restrictions. The Legislature had unlimited borrowing power which was extended to a myriad of public works projects—canals and railroads were the principal items. When these over-optimistic investments in Pennsylvania and other states failed and defaults became common in the late 1830's and early 1840's, the public expressed its resentment by amending the State Constitutions to prevent further legislative abuse of the borrowing power. In 1842, Rhode Island passed the first such amendment which restricted legislative borrowing to \$50,000 without

the consent of the voters except for invasion, insurrection or in time of war. By 1857, when Pennsylvania voters imposed its constitutional restrictions, 18 other states had already passed similar limitations. The 1857 amendment restricted the amount of debt to \$750,000 and the 1873 Convention raised this amount to \$1 million almost without comment.

The only amendments to Section 4 have been a 1918 amendment which added a provision authorizing the State to issue bonds for highway improvement not to exceed fifty million dollars and a 1923 amendment which increased the bond limit to one hundred million dollars.

Judicial Interpretations

The Courts give force to the debt limitation provisions of Section 4 by interpreting them as invalidating any appropriations which are over one million dollars in excess of estimated annual revenues available to meet those appropriations plus any surplus (or less any deficit) on hand at the beginning of the year.⁶ In determining whether a given appropriation is valid, the Courts said that preference must be given to appropriations covering the expenses of the executive, judicial and legislative departments of the government and the expenses of the public schools. Other appropriations are abated pro rata unless the Legislature has intended that certain appropriations shall be preferred.⁷

The Courts have limited the effect of Section 4 by excluding two types of indebtedness from its coverage. The most significant are authority bonds and leaseholds arising out of authority financing. The Court decisions held that neither the bonds issued by the authority nor the long-term leasehold between the authority and the State constitutes debt under Section 4.⁸ The long-term leasehold does not constitute debt of the State according to the decisions because the State pays as it goes, receiving consideration for each payment as it falls due; there is no surcharge on the credit of the future, and the bonds do not constitute State debt because they are not backed by State credit or property.

The second type of State indebtedness excluded by the judicial interpretation of Section 4 as not constituting debt is the tax anticipation notes issued by the State to defray current expenses which will eventually be discharged from money received from revenues already provided for and to become receivable in the current year.⁹

The only other relevant case involving Section 4 is a Pennsylvania Supreme Court decision construing the proviso relating to the one-hundred million dollar debt for highways as permitting only one issue of State bonds to the amount of one-hundred million dollars and not as fixing a given borrowing capacity for highway improvement.¹⁰ Thus, for practical purposes this provision has no current application.

Debt Limitations in Other States

There are three major categories into which states can generally be divided concerning the incurrence of public debt: (1) States which must amend their constitutions to authorize borrowing except for certain limited purposes or amounts. Ratification by the voters is required in each case. Nineteen states (including Pennsylvania) fall into this category. (2) States whose electorate must ratify legislation authorizing borrowing. Twenty-two states fall into this category including several having the newer constitutions (Alaska—1958; Michigan—1963; New Jersey—1947). (3) States without substantial debt limitations. Eight states fall into this category. In addition, Hawaii's Constitution permits the borrowing of up to \$60 million by legislative enactment and an added amount up to the equivalent of 15 percent of the assessed valuation of taxable real estate when approved by a two-thirds vote of all the authorized members of both houses.

An examination of the debt records of the states indicates that constitutional provisions restricting debt appear to have had an effect upon the amount of debt incurred, even where these restrictions can be avoided through the use of the authority mechanism. Table 4 summarizes long-term state debt of the states, broken down into the three categories mentioned

TABLE 4: LONG-TERM STATE DEBT—1966¹¹

	<i>No Refer- endum or Constitutional Amendment</i>	<i>Popular Refer- endum Only</i>	<i>Constitutional Amendment</i>	<i>Pennsylvania</i>
Per Capita—Long-Term Debt	\$281.23	\$129.23	\$100.94	\$165.69
Per Capita—Non-Guaranteed Debt	\$ 81.22	\$ 77.14	\$ 68.71	\$150.26
Percent of Non-Guaranteed Long-Term Debt to the Total	34.5 %	49.7 %	77.5 %	90.0 %

Source: U.S. Bureau of the Census, *State Government Finances in 1966*.

above, and of Pennsylvania. The three tabulations which follow show the long-term debt of the states, that portion of the total long-term debt that is not guaranteed and the per capita debt in both instances. Table 5 reports the debt records of 19 states, including Pennsylvania, in which a constitutional amendment is required to incur debt; Table 6 is the debt record of 22 states which require only popular referendum; and Table 7 shows the debt record of nine states where debt may be incurred by legislative action only, without constitutional amendment or referendum.

Analysis of the summary in Table 4 reveals that states requiring constitutional amendments do have the lowest long-term per capita debt—\$100.94

TABLE 5. DEBT RECORD OF 19 STATES WHERE A CONSTITUTIONAL AMENDMENT IS REQUIRED TO INCUR DEBT—1966

State	Purpose of Debt*	Maximum Legislative Borrowing	Total Long-Term Debt (000)	Non-Guaranteed Long-Term Debt Amount (000)	Percent of Total Long-Term Debt	Per Capita Total Long-Term Debt (Dollar Amts.)	Per Capita Non-Guaranteed Debt
Alabama	A	\$ 300,000	\$497,162	\$445,362	89%	\$141.36	\$126.63
Arizona	B	350,000	45,697	45,697	100	28.24	28.24
Colorado	A	850,000	120,460	120,460	100	60.93	60.93
	C	50,000					
		2,115,000					
Florida		No-Borrowing	795,005	795,005	100	133.82	133.82
Georgia	C	3,500,000 Payment Teachers	590,457	590,441	99	132.42	132.42
	B	500,000 Unrestricted					
	A	Unlimited					
Indiana		No Borrowing otherwise	498,788	498,633	99	101.42	101.39
Louisiana	AC	2,000,000	646,307	280,537	43	179.38	77.86
Minnesota	C	250,000	315,630	43,053	13	88.26	12.04
Nebraska	A	100,000	65,706	65,706	100	45.13	45.13
Nevada	A	1% Assessed Value	15,942	6,237	39	35.11	13.74
North Dakota	B	2,000,000	24,822	22,235	89	38.19	34.21
Ohio	AB	750,000	870,418	786,321	90	84.47	76.30
Oregon	A	50,000	452,558	40		231.49	.02
Pennsylvania	A	1,000,000	1,919,004	1,740,263	90	165.69	150.26
South Dakota	AC	100,000	19,021	19,021	100	27.89	27.89
Texas	A	200,000	609,994	330,969	54	56.73	30.78
Utah	AB	1-1/2% Assessed Value	106,854	39,854	37	106.01	39.54
	A	Unlimited					
West Virginia	A	No Borrowing otherwise	348,702	264,187	75	194.37	147.26
Wisconsin	C	100,000	278,941	278,941	100	67.04	67.04
Average			\$ 432,709	\$ 335,419	77.5%	\$100.94	\$ 68.71

Source: U.S. Bureau of the Census, *State Government Finances in 1966*

TABLE 6. DEBT RECORD OF 22 STATES WHERE POPULAR REFERENDUM ONLY IS REQUIRED
(NO CONSTITUTIONAL AMENDMENT)

24

State	Purpose of Debt*	Maximum Legislative Borrowing	Total Long-Term Debt (000)	Non-Guaranteed Long-Term Debt Amount (000)	Percent of Total Long-Term Debt	Per Capita Total Long-Term Debt Dollar Amts.)	Per Capita Non-Guaranteed Debt
Alaska		None	\$ 62,085	\$ 26,550	43.0%	\$228.25	\$ 97.81
Arkansas		None	105,927	68,684	64.0	54.18	35.13
California	B	\$ 300,000	4,201,494	335,121	7.9	222.09	17.71
Idaho	B	2,000,000	15,625	14,629	90.0	22.51	21.08
Illinois	A	250,000	1,147,082	770,351	67.0	106.98	71.85
Iowa	AB	250,000	70,412	50,857	72.0	25.63	18.51
Kansas	C	1,000,000	251,422	233,068	92.6	111.74	103.59
Kentucky	A	500,000	839,263	594,673	70.0	263.67	186.83
Maine	B	2,000,000	160,518	81,714	50.9	163.29	83.13
Michigan		None	942,707	884,257	93.0	112.58	105.60
Missouri	AC	1,000,000	130,973	82,423	63.0	29.05	18.28
Montana	B	100,000	72,774	71,023	97.5	103.67	101.17
New Jersey	B	1% of Year's Total Approp.	1,022,225	486,075	47.5	148.19	70.47
New Mexico	AB	200,000	124,562	101,341	82.0	121.88	99.16
New York		No Borrowing	4,206,531	2,527,923	60.0	230.39	138.46
North Carolina	A	Unlimited for Casual Deficits					
	B	Other— ² / ₃ of amount by which outstanding indebted- ness was reduced in preceding biennium	274,350	58,660	21.0	50.87	11.73
Oklahoma	A	500,000	415,882	331,657	79.0	169.20	134.93
Rhode Island	B	50,000	240,972	46,354	19.0	268.34	51.62
South Carolina		No Borrowing Except for Ordinary and Current Business	238,670	67,943	28.0	92.29	26.27

Virginia	A	Unlimited					
		No-Borrowing otherwise	276,599	275,530	99.0	61.37	61.13
Washington	AB	400,000	540,673	497,961	92.0	181.43	167.10
Wyoming	B	1% of Assessed Valuation	24,857	24,857	100.0	75.55	75.55
Average			\$ 698,436	\$ 346,893	49.7%	\$129.23	\$ 77.14

Source: U.S. Bureau of the Census, *State Government Finances in 1966*

*A Casual deficits; B Unrestricted; C Specified Purpose, Other

TABLE 7. DEBT RECORD OF STATES WHERE LEGISLATURE
MAY INCUR DEBT WITHOUT REFERENDUM OR CONSTITUTIONAL AMENDMENT

State	Maximum Legislative Borrowing	Total Long-Term Debt (000)	Non-Guaranteed Long-Term Debt Amount (000)	Percent of Total Long-Term Debt	Per Capita Total Long-Term Debt (Dollar Amts.)	Per Capita Non-Guaranteed Debt
Connecticut	Unlimited	\$1,091,104	\$336,441	30.0%	\$379.51	\$117.02
Delaware	Unlimited	334,452	77,659	23.0	653.23	151.68
Hawaii	Unlimited	302,749	93,686	31.0	421.66	130.48
Maryland	Unlimited	813,431	438,872	53.0	225.14	121.47
Massachusetts	Unlimited	1,733,573	684,483	39.0	332.05	127.16
Mississippi	Unlimited	251,355	127,523	50.0	108.02	54.80
New Hampshire	Unlimited	115,300	3,238	2.0	169.31	4.75
Tennessee	Unlimited	196,935	20,745	10.0	50.72	5.34
Vermont	Unlimited	77,551	7,412	9.0	191.48	18.30
Average		\$ 546,272	\$198,895	34.5%	\$281.23	\$ 81.22

Source: U.S. Bureau of the Census, *State Government Finances in 1966*

—and the highest percent (77.5 percent) of this total is in the nonguaranteed class. Totals for the group requiring constitutional amendment are only reasonably lower than those requiring referendum but the per capita average is 64 percent lower than the unrestricted states—\$100.94 compared with \$281.23.

Table 5 reveals that 12 of 19 states requiring constitutional amendments have 89 percent or more of their debt in the nonguaranteed class.

The voters in other states, as in Pennsylvania, do not consistently support proposed bond authorizations. A special study of a six-year period between 1957 and 1962 showed that 97 proposed bond issues (excluding proposals for veteran's bonuses) were submitted to the voters of 18 states. The voters approved 72 issues amounting to \$6,313,175,000 and rejected 25 issues amounting to \$1,753,430,000, or 74 percent of the projects involving 78 percent of the total amounts submitted.

This study indicated that the voter's decision to approve or reject bond proposals appears to be based upon special circumstances surrounding a particular project. It did not reveal any definite patterns which would show that the voters are generally influenced by the purpose of the authorization, the size of the bond issue, or the frequency of bond proposals in the State.

Alternatives

Irrespective of constitutional regulations, it will undoubtedly be necessary for the State to continue to finance a major portion of its capital needs through borrowing. Thus, as a practical matter the issue facing the Convention is not whether to abolish borrowing as a means of financing capital improvements but the degree to which the electorate should directly participate in borrowing decisions. The following alternatives are available to the Convention:

1. *Require a Constitutional amendment for the incurrence of all State debt including authority financing.*

A constitutional provision prohibiting all State debt, would continue the difficult route of Constitutional amendment for each borrowing program. If such an amendment included authority borrowing, the State's capital program could be radically slowed or stopped.

Nineteen states, including Pennsylvania, require a Constitutional amendment for direct State borrowing.

2. *Permit borrowing by action of the Legislature with voter approval.*

The *Report of the Commission on Constitutional Revision (1959)* and the *Report of the Governor's (Scranton) Commission on Constitutional Revision (1964)* recommended that Section 4 be altered to permit the creation of debt for capital improvement upon voter ratification of legislation providing for such debt and to eliminate most authority financing by prohibiting issuance of authority debt involving leases with the Commonwealth, the rentals of which are payable out of general revenues.

The Pennsylvania Bar Association also proposed the amendment of Section 4 to permit the creation of debt for capital improvement upon voter ratification of legislation providing for such debt. Its proposal differed from the previous proposal in that, inter alia, it did not prohibit authority financing.

Twenty-two states permit borrowing with voter approval. One of the more modern constitutions following this path is Alaska's Constitution.

Alaska—State Debt: No State debt shall be contracted unless authorized by law for capital improvements and ratified by a majority of the qualified voters of the State who vote on the question. The State may, as provided by law and without ratification contract debt for the purposes of repelling invasion, suppressing insurrection, defending the State in war, meeting natural disasters, or redeeming indebtedness outstanding at the time this Constitution becomes effective (Article IX, Section 8).

The difference between this alternative and the previous one is that while both preserve the requirement of voter ratification of legislation proposing to create debt for capital improvement, this second alternative does not require an amendment to the Constitution and thus permits the creation of debt for capital improvements in a much shorter time and does not clog up the Constitution with numerous amendments.

3. *Eliminate All Constitutional Controls Over the Authorization of Debt*

This directly opposite alternative permits the Legislature to borrow as it sees fit so long as the projects are clearly specified.

Eight state constitutions follow this course. In addition, this is the recommendation of the Model State Constitution;

"No debt shall be contracted by or in behalf of this State unless such debt shall be authorized by law for projects or objects distinctly specified therein."¹²

Such a provision would obviously negate any need for authority borrowing.

4. *Provide Limited Freedom to Legislature*

The Convention may decide that it is advisable to give the Legislature some freedom to incur indebtedness but also to impose certain restrictions. There are many provisions which will accomplish this in varying degrees.

One possibility would follow the pattern now authorized by the Constitution for capital improvements by local governments which grants a minimum amount (five percent of assessed value) to be borrowed entirely at the discretion of the governing body—council, school board, etc. and an additional amount (15 percent of assessed valuation) to be borrowed with the approval of the electorate. This gives some flexibility to the incurring of debt without relinquishing control entirely.

Since the State does not tax real estate, however, some other flexible measures have been suggested. One proposal would permit the Legislature to borrow for capital expenditures up to one-half of the current operating

budget; another would make the limitation "an amount which could be financed by ten percent of the average uncommitted general fund revenues for the past five years."¹³ Both these proposals would permit additional borrowing for specific projects upon voter ratification.

Another possibility is the establishment of special procedural requirements for approval of debt, such as a two-thirds or three-fifths vote of the Legislature. Such a provision would tend to hold the domination of the majority party to a minimum because legislators of both parties probably would have to support each borrowing program.

Still another possibility is to prohibit borrowing to pay current expenditures, including the debt service covering interest and principal payments on outstanding indebtedness, but to permit unlimited borrowing by the Legislature to finance capital improvements. The rationale for prohibiting borrowing for current expenditures is that a "pay-as-you-go" philosophy is defensible for current expenditures, the benefits of which are enjoyed immediately. Sufficient funds for capital improvements on the other hand cannot be raised from current revenues and in addition, it is consistent with a "pay-as-you-go" philosophy to pay off such improvements over their useful life.

One more possibility is the present solution in Pennsylvania of prohibiting borrowing but not extending this prohibition to authority financing. This gives the Legislature almost unrestricted freedom to finance capital improvements through authority borrowing but almost no opportunity to finance current expenditures through borrowing. The weakness of this solution is that it results in the use of less economical authority financing. So long as the Legislature has the power to finance capital improvements through borrowing, there is no reason why it should not have the power to do so through the more economical method of direct state borrowing.

The merits of the various alternatives depend upon the extent to which it is believed that restrictions should be placed upon the Legislature's power to incur debt for capital improvements.

Arguments cited in favor of requiring electorate approval of legislation providing for the creation of debt include:

Because of its long-term commitment, debt financing should be treated with greater restraint than current tax financing and the referendum requirement is the only method by which the people can restrain the creation of long-term debt. Without the referendum requirement, a temporary majority in the Legislature could burden the taxpayers with a heavy debt for an extended period of years.

Because it is more expedient politically to propose the creation of new debt rather than to increase taxes, a governor or legislature might rely too heavily on long-term debt financing if the creation of debt were made easier through the elimination of the referendum requirement:

A state does not have the deficit financing and fiscal mechanisms avail-

able to the federal government. Thus it is important for the people to be able to protect themselves from well-meaning public officials who want public improvements so badly that they do not give adequate concern to the financing of these improvements.

Such a requirement is necessary to protect the credit rating of the State, thus enabling the State to borrow funds at low rates of interest.

Arguments cited in favor of removing the restrictions on the power of the Legislature to create debt for capital improvements include:

Through authority financing the Legislature since 1935 has had almost unrestricted power to finance capital improvements with borrowed funds. This shows that restrictions on the power of the Legislature to borrow funds for capital improvements are no longer necessary.

It is frequently difficult to obtain voter approval for borrowing to finance capital improvements deemed necessary by the Governor and Legislature because the voters are unaware of the necessity for such improvements. The voters haven't the same opportunity as their legislators to become sufficiently informed on such matters. Consequently, the Legislature should be given the power to act on behalf of the people on such matters.

The delay caused by the referendum procedure may be detrimental when speed is necessary to take advantage of a favorable bond market or to start a project of immediate necessity to the welfare of the Commonwealth.

Reporting by the news media, pressure from interested groups, and the necessity to find buyers for bonds operate as a sufficient check to prevent irresponsible deficit financing.

Debt restrictions too rigidly curtail borrowing necessary to finance capital improvements that are needed to attract and retain industry to the State. Borrowing for such purposes is a wise investment that will reap large dividends in terms of an expanded economy and hence a larger tax base.

In the long run, restrictions tend to be countered by evasions as is evidenced by the extensive use of the authority mechanism in this State. It is far better to have a forthright and coherent debt policy, using the appropriate means for funding capital improvements, than one which invites circumventions and ad hoc arrangements.¹⁴

Indebtedness Authorized by Constitutional Amendment

As was previously stated, since 1874 there have been ten amendments to the Constitution authorizing the creation of debt for certain specified purposes. These amendments are listed below:

<i>Section</i>	<i>Date</i>	<i>Amount</i> 000,000	<i>Purpose</i>
4	1918	\$ 50	highway construction
4	1923	\$ 50	highway construction
16	1933	\$ 50	Veterans' bonus—World War I, etc.

<i>Section</i>	<i>Date</i>	<i>Amount</i> 000,000	<i>Purpose</i>
16	1933	\$ 10	acquisition of toll bridges
17	1933	\$ 25	defray governmental expenses
21	1945	\$ 50	certain public works projects
22	1949	\$ 500	Veterans' bonus—World War II
23	1957	\$ 150	Veterans' bonus—Korean War
24	1963	\$ 70	conservation
25	1967	\$ 500	conservation

With respect to the proviso to Section 4 relating to highway financing and Sections 16, 16, 17, 21, 22, and 23, the programs and purposes for which such borrowing is authorized have been completed. Because these amendments serve no function today, the *Report of the Commission on Constitutional Revision (1959)*, the *Report of the Governor's (Scranton) Commission on Constitutional Revision (1964)* and the Pennsylvania Bar Association have recommended their repeal.¹⁵

The Legislature, on the other hand, has not completed the programs for which the borrowing is authorized by Section 24 and 25 and almost certainly will wish to incur indebtedness pursuant to the authority created in these Sections to finance these programs. Thus these Sections should be left in their present form unless the Section relating to State indebtedness is amended to authorize the Legislature to incur the indebtedness for projects previously approved by the electorate, in which case Sections 24 and 25 may be repealed. This latter alternative is favored by the *Report of the Governor's (Scranton) Commission on Constitutional Revision (1964)* and the Pennsylvania Bar Association.

PURPOSES OF BORROWING MUST BE SPECIFIED

Background

Another restriction on the power of the Legislature to manage the State's finances is imposed by Section 5 of Article IX which requires legislation authorizing the creation of debt to specify the purpose for which the money is to be used. This Section reads as follows:

All Laws, authorizing the borrowing of money by and on behalf of the State, shall specify the purpose for which the money is to be used, and the money so borrowed shall be used for the purpose specified and no other.

This Section was part of the original 1874 Constitution and has never been amended. Previously, Article 11, Sections 1 and 2 of the 1838 Constitution had required that money raised from debt authorized by the Constitution be applied "to the purposes for which they were raised or to repay such debts and to no other purposes whatever."

The Pennsylvania Supreme Court has construed Section 5 as demanding "that every act which authorizes the creation of a debt shall state distinctly,

without reference to other sources of information, a single purpose for which the money is to be borrowed."¹⁶

Today the Section has limited significance. It does not apply to authority financing because such financing does not constitute a debt of the State. And all other borrowing by the State is pursuant to Constitutional amendments which specify the purpose for which the debt may be created. The Section would assume much greater significance if, by Constitutional amendment, the Legislature were given additional power to create debt.

The requirements imposed by Section 5 are not unique. The constitutions of approximately twenty other states, as well as the Model State Constitution, similarly require statutes authorizing the creation of debt to specify distinctly the purpose for which the borrowed funds are to be used.

Alternatives

The Convention has basically two alternatives: to keep the requirement limiting each debt proposition to a single purpose or to remove the requirement and thus permit the Legislature to authorize general borrowing for a variety of purposes.

The first alternative is favored by the *Commission on Constitutional Revision* (1959) which proposed no change to Section 5 and by the *Report of the Governor's (Scranton) Commission on Constitutional Revision* (1964) and the Pennsylvania Bar Association which proposed the repeal of Section 5 and including in the section dealing with State debt the requirement that capital improvements be specified separately in any statute authorizing borrowing to finance capital improvements.

The arguments in favor of the single purpose limitation are that multi-purpose debt does not give the voters the opportunity to choose specific projects to approve or reject; that if the single purpose limitation were abolished, the Legislature could lump enough local or minor projects together to gain passage of a bond authorization where each or at least many of these projects would be rejected if voted on separately; that while the single purpose limitation enables the voters to have a general knowledge of the purposes for the borrowing, it still permits the authorization of a bond issue for a series of projects accomplishing one purpose—a separate bond issue isn't needed for each project, and that the legislative restriction upon the Executive Department's administration of the capital funds provided by the single purpose limitation results in more sound financing of capital improvements.

The arguments in favor of the multi-purpose debt are that the single purpose limitation fragments the State's borrowing—it must plan and fund each project and purpose in isolation and cannot weigh the benefits of one purpose against those of another when it allocates borrowed funds; and that the single purpose limitation restricts the flexibility of the State to alter its plans as conditions change during the frequently lengthy time period involved in completing capital improvements.

SINKING FUND REQUIREMENTS

Section 11 of Article IX requires the Legislature to maintain a sinking fund sufficient to pay the accruing interest on the State debt and to reduce the principal thereof annually by a sum not less than \$250,000.

The Section reads as follows:

To provide for the payment of the present State debt, and any additional debt contracted as aforesaid, the General Assembly shall continue and maintain the sinking fund, sufficient to pay the accruing interest on such debt, and annually to reduce the principal thereof by a sum not less than two hundred and fifty thousand dollars; the said sinking fund shall consist of the proceeds of the sales of the public works or any part thereof, and of the income or proceeds of the sale of any stocks owned by the Commonwealth, together with other funds and resources that may be designated by law, and shall be increased from time to time by assigning to it any part of the taxes or other revenues of the State not required for the ordinary and current expenses of government; and unless in case of war, invasion or insurrection, no part of the said sinking fund shall be used or applied otherwise in the extinguishment of the public debt.

This section was part of the original 1874 Constitution and has never been amended. Article 11, Section 4 of the 1838 Constitution embodied a similar provision.

The purpose of the sinking fund requirement is to insure payment of the State debt which in turn permits the State to borrow at lower interest rates. Approximately one-half of the state constitutions contain some provision requiring appropriations for the payment of the State debt.

There have been no proposals to abolish or ease the sinking fund requirements. In fact, the *Report of the Commission on Constitutional Revision* (1959), the *Report of the Governor's (Scranton) Commission on Constitutional Revision* (1964) and the Pennsylvania Bar Association all recommend an amendment to Section 11 which would strengthen these requirements by requiring the Legislature to maintain a sinking fund sufficient to pay the principal as well as the interest on the State debt and by requiring the State Treasurer to set aside funds sufficient to make such principal and interest payments if the Legislature at any time failed to make sufficient appropriations for this purpose. The reason for this recommendation is to improve the State's credit rating and thus permit the State to borrow at lower rates of interest.

SURPLUS FUNDS

Restrictions limiting the amount of the State's reserve funds to moneys required for current expenses, requiring all other funds to be used to pay State debt either directly or through the sinking fund, and requiring the funds in the sinking fund to be invested only in bonds of the United States and Pennsylvania are contained in Sections 12 and 13 of Article IX which read as follows:

Section 12

The moneys of the State, over and above the necessary reserve, shall be used in the payment of the debt of the State, either directly or through the sinking fund, and the moneys of the sinking fund shall never be invested in or loaned upon the security of anything, except the bonds of the United States or of this State.

Section 13

The moneys held as necessary reserve shall be limited by law to the amount required for current expenses, and shall be secured and kept as may be provided by law. Monthly statements shall be published showing the amount of such moneys, where the same are deposited, and how secured.

Both these sections were part of the original 1874 Constitution and have not been amended. The Constitution of 1838 contained no equivalent provisions.

These provisions were added to the Constitution in 1874 to eliminate investment of State surpluses in private corporations. In the period around 1873, surpluses were the rule rather than the exception and frequently these surpluses had been invested in private corporations to the detriment of the public interest.

The requirements imposed by Section 12 are favored by the *Report of the Commission on Constitutional Revision (1959)* which recommended no changes to the Section and by the *Report of the Governor's (Scranton) Commission on Constitutional Revision (1964)* and the Pennsylvania Bar Association which proposed only one minor change to the Section—the substitution of the term “Obligations” for the term “bonds” in order to permit the State to invest the moneys in the surplus fund in other types of obligations of the United States and Pennsylvania, such as treasury notes, certificates and bills.

The above studies, on the other hand, all recommended the repeal of Section 13. The reason given for such a recommendation was that while this Section is of little consequence today because Pennsylvania is presently faced with managing deficits rather than surpluses, a time may come when surpluses will occur and if it does the State should be in a position to provide for the orderly development of a capital improvements program through the establishment of a capital reserve fund. Such action is, however, prohibited by Section 13.

STATE CREDIT NOT TO BE PLEDGED

Section 6 of Article IX prohibits the pledging of the State credit to any private body. This Section reads as follows:

The credit of the Commonwealth shall not be pledged or loaned to any individual, company, corporation or association, nor shall the Commonwealth become a joint owner or stockholder in any company, association or corporation.

This section was part of the original 1874 Constitution and has not been amended. Article XI, Section 5 of the 1838 Constitution embodied substantially the same proposition.

Most states have provisions of this nature in their constitutions. Some of these provisions, however, contain specific exemptions from the restriction. There have been no proposals to repeal or change this Section.

PUNISHMENT FOR MISUSE OF STATE FUNDS

Section 14 of Article IX provides that the misuse of State funds by any State officer or member of the General Assembly shall constitute a misdemeanor and part of such punishment shall be disqualification from office for at least five years. This Section reads as follows:

The making of profit out of the public moneys or using the same for any purpose not authorized by law by any officer of the State, or member or officer of the General Assembly, shall be a misdemeanor and shall be punished as may be provided by law, but part of such punishment shall be disqualification to hold office for a period of not less than five years.

This section was part of the original 1874 Constitution and has not been amended. The 1838 Constitution contained no equivalent provision.

There have been no proposals to repeal or change this Section.

Notes to Chapter 2

1. By a 1967 amendment to the Constitution (Section 1 (a) of Article XVIII) more prompt amendment of the Constitution is possible in the event a major emergency threatens the State and the welfare of the State requires prompt amendment of the Constitution. In this case an amendment, if approved in a single session by two-thirds of the members of the House of Representatives and Senate, may be submitted to the electorate for final approval within one month thereafter. The requirement that the amendment be necessary because of a major emergency will probably prevent the use of this Section for most amendments authorizing borrowing for capital improvements.
2. This restriction is continued in Section 1 of Article XVIII
3. The debt totals of the following authorities are often included in summary totals of debt outstanding, but they are not State obligations:
The Pennsylvania Turnpike Commission and the Delaware River Port Authority had outstanding indebtedness of \$331 million and \$110 million, respectively. This will be paid from tolls.
The State Public School Building Authority had an outstanding indebtedness of \$474 million. Most of this will be paid from rentals derived from long-term leaseholds with local school districts.
4. Kurtzman, David H., *The Impact of Constitutional Debt Limitation on Financing Capital Improvements in Pennsylvania*, 1963.
5. *ibid.*
6. *Kelley v. Baldwin* 319 Pa. 53, 62 (1935)
7. *Commonwealth ex. rel. Schnader v. Liveright* 308 Pa. 35, 67-69 (1932)
8. *Kelley v. Earle* 325 Pa. 337 (1937)
9. *Kelley v. Baldwin* 319 Pa. 53 (1935)
10. *Montgomery v. Martin* 294 Pa. 25 (1928)
11. *State Government Finances in 1966*, U.S. Dept. of Commerce, Bureau of the Census, 1967.
12. *Model State Constitution*, National Municipal League, Sixth Edition 1963, Article VII, Section 1.

13. The first proposal was made by the Kurtzman Study. This proposal, today, would make possible borrowing without voter approval of more than \$800 million. The second proposal was made by the Modern Constitution for Pennsylvania, Inc., which estimated this formula would allow about \$60 million for debt service which at present rates should finance borrowing between \$818 and \$984 million.
14. Many of the arguments setting forth the advantages and disadvantages of borrowing restrictions were taken from Report 8, *State Finance*, prepared by the Temporary State Commission on Constitutional Revision for New York (1967).
15. The *Report of the Commission on Constitutional Revision (1959)* did not recommend the repeal of Article 23 because at the time the Commission met borrowing for the payment of bonuses to Korea War Veterans was not complete.
16. *Hollinger v. King* 282 Pa. 157, 163 (1925).

CHAPTER 3

The State Budget

Debt for Casual Deficiencies

“... and the debt created to supply deficiencies in revenue shall never exceed, in the aggregate at any one time, one million dollars...” (Section 4, Article IX).

INTRODUCTION

There has been, over the years, much caustic comment about the Pennsylvania million dollar debt limit, but in effect this requirement has served in recent years as the constitutional requirement for the preservation of a balanced budget.

The \$1 million limit on the incurring of debt for casual deficiencies in revenue has been interpreted by the courts (*Commonwealth v. Liveright*, 308 Pa. 35-1932) as invalidating appropriations which are more than \$1 million in excess of estimated resources available to meet those appropriations. A million dollars might have given some leeway to the Legislature and the Governor in 1873 when the annual budget was less than \$7 million but it has lost its flexibility for today's annual budget of \$2-1/2 billion with \$1-1/2 billion in the General Fund alone.

If the Convention were to repeal or substantially change the present debt section it would be appropriate to consider its effect on the State's fiscal policy.

HISTORY

Pennsylvania was not among the pioneers in the development of the executive budget—Ohio in 1910 and Maryland in 1916 were the forerunners. The Sproul Commission in 1919 proposed an executive budget to, among other things, increase the Governor's power, but no changes occurred until the enactment of the Administrative Code of 1923. This act placed the preparation and execution of the budget under the governor with an allotment

system to strengthen his control. Timetables for the preparation and review of agency spending were established. The establishment of a Budget Bureau followed in 1927 and the process was strengthened and clarified in the *Administrative Code of 1929 under which the State operates today*.

It has been observed that fixed provisions of the constitution have established no insurmountable obstacles to the development of a modern budgetary system. However, taxing and borrowing restrictions have reduced the State's flexibility in the development of a capital improvement program.

STATE BUDGET PRACTICE

There is some disagreement among students of the subject as to the necessity for a constitutional provision establishing the budget.

There is further difference of opinion as to whether this or any other constitutional provision should speak in brief general terms or detail some of the procedures.

In general, governmental budgetary procedure has been described as a process which,

involves the bringing together of estimates covering the multifarious needs of a government, the checking of these estimates against recorded expenditure data, the calculation of the government's income in the light of past experience, the preparation of the budget and supporting measures by the responsible executive or other agency of the government, the adoption of the budget and the enactment of the bills designed to carry it into operation by the legislative body and finally, the execution of the budget by the executive or the administration officer in accordance with the authorization of the legislative body.¹

All the states including Pennsylvania follow a budget procedure similar to this now old but valid description, although there is little consistency of organization or effectiveness among them.

While all states now have a budget, only 42 have an executive budget and only 16 of these are provided for by their respective state constitutions.

Among the states with constitutional provisions for a budget, there is no real uniformity. States such as Maryland and Oklahoma spell out many limitations in an effort to guarantee fiscal responsibility, while others like Alaska and Hawaii adopt almost the identical wording of the Model State Constitution² which speaks in very general terms:

Section 7.02. The Budget. The governor shall submit to the Legislature, at a time fixed by law, a budget estimate for the next fiscal year setting forth all proposed expenditures and anticipated income of all departments and agencies of the state, as well as a general appropriation bill to authorize the proposed expenditures and a bill or bills covering recommendations in the budget for new or additional revenues.

It is worth noting that all of the more recently adopted constitutions—Michigan, Missouri, New Jersey, Hawaii, Alaska contain strong budget provisions, and that similar strong provisions are being proposed in New York and Maryland.

The most recently adopted constitution—Michigan—sets forth in considerable detail the responsibilities of the Governor in the fiscal process.

Section 18. Governor; budget and appropriations. The governor shall submit to the legislature at a time fixed by law, a budget for the ensuing fiscal period setting forth in detail, for all operating funds, the proposed expenditures and estimated revenue of the state. Proposed expenditures from any fund shall not exceed the estimated revenue thereof. On the same date, the governor shall submit to the legislature general appropriation bills to embody the proposed expenditures and any necessary bill or bills to provide new or additional revenues to meet proposed expenditures. The amount of any surplus created or deficit incurred in any fund during the last preceding fiscal period shall be entered as an item in the budget and in one of the appropriation bills. The governor may submit amendments to appropriation bills to be offered in either house during consideration of the bill by that house, and shall submit bills to meet deficiencies in current appropriations. (Article V, Section 18)

The obligations of the Legislature are similarly spelled out.

Section 31. General appropriation bills. The general appropriation bills for the succeeding fiscal period covering items set forth in the budget shall be passed or rejected in either house of the legislature before that house passes any appropriation bill for items not in the budget except bills supplementing appropriations for the current fiscal year's operation. Any bill requiring an appropriation to carry out its purpose shall be considered an appropriation bill. One of the general appropriation bills as passed by the legislature shall contain an itemized statement of estimated revenue by major source in each operating fund for the ensuing fiscal period, the total of which shall not be less than the total of all appropriations made from each fund in the general appropriation bills as passed.

THE BUDGET AND THE PENNSYLVANIA CONSTITUTION

There is no budget article as such in the present Pennsylvania constitution. While the Constitutional Convention of 1874 was called primarily to limit questionable legislative financial practices, there was no inclination to weaken the general policy making control of the Legislature.³

The constitutional provisions for the general appropriation bill and all other appropriation bills along with the statute regulating the paying out of public funds are located in the Article defining legislative powers. Also, the provision that all bills for raising revenue must originate in the House of Representatives is contained in the same article.

11. Appropriation bills. The general appropriation bill shall embrace nothing but appropriations for the executive, legislative and judicial departments of the Commonwealth for the public debt and for public schools. All other appropriations shall be made by separate bills, each embracing but one subject.

(Amendment of May 16, 1967).

(Formerly Article III, Section 15.)

24. Paying out public moneys; cash refunds. No money shall be paid out of the treasury, except on appropriations made by law and on warrant issued by the proper officer; but cash refunds of taxes, licenses, fees and other charges paid or collected,

but not legally due, may be paid as provided by law, without appropriation from the fund into which they were paid, on warrant of the proper officer.

(Renumbered May 16, 1967).
(Formerly Article III, Section 16.)

14. Revenue bills. All bills for raising revenue shall originate in the House of Representatives, but the Senate may propose amendments as in other bills.

The Governor's power and responsibilities in the fiscal area arise from his position as Chief Executive and are set forth by the Legislature in the Fiscal Code of 1929. His veto powers are contained in Article IV of the Constitution under his powers as the Chief Executive. His item veto⁴ for appropriation bills gives him more power than most Chief Executives.

Section 16. The Governor shall have power to disapprove of any item or items of any bill, making appropriations of money, embracing distinct items, and the part or parts of the bill approved shall be the law, and the item or items of appropriation disapproved shall be void, unless re-passed according to the rules and limitations prescribed for the passage of other bills over the Executive veto.

These sections, along with the debt limitations, form the constitutional base for state financial operation.

None of these provisions are in sections designated for revision by the bill authorizing this convention, but, if Section 4 of Article IX is to be changed, the questions to be resolved by the Constitutional Convention would seem to be:

- (1) whether there should be any constitutional limitation on the State's power to incur debt for balancing the budget,
- (2) whether the present one million dollar limitation should remain,
- (3) whether the Constitution should prohibit such borrowing for current expense in any amount, or
- (4) whether there should be a more positive budget provision rather than negative debt limitation.

If the determination is to include a "budget" provision, it could be included as a part of a new State finance section, assuming this to be an Article within the Convention's jurisdiction.

THE PRESENT PENNSYLVANIA BUDGET

Almost every administration within recent years has seen the Governor and Legislature engaged in a prolonged struggle before the essentials of a fiscal program could be agreed upon.

Budget balancing is not easy in a decade when the General Fund Budget for the 1955-57 *biennium* (\$1.27 billion) was substantially less than the *annual* budget for 1966-67 of \$1.46 billion. Yet such a rapid increase might make some positive control mechanism essential.

In arriving at a decision regarding the needs for such controls, it is important to ascertain the extent to which the present constitutional provision

has actually prevented deficit financing. For this purpose, an analysis has been made of the Commonwealth's general fund operations for the past 14 years. The closing surplus or deficit is indicated in millions of dollars.

*For Biennia ending May 31, from 1955 thru 1961,
and for Fiscal years ending June 30, since 1962*

1953-55	(\$ 52.3)
1955-57	(52.5)
1957-59	(141.9)
1959-61	(33.3)
1962	16.6
1963	(14.5)
1964	29.3
1965	106.4
1966	134.3
1967	99.0

There was a deficit in each of the last four biennial fiscal periods, 1953-55 to 1959-61, followed by a surplus in five out of six years since the State began operating on a single fiscal year with annual sessions of the Legislature.

In view of the size of the variation from a \$141.9 deficit to a \$134.3 surplus, it is questionable whether the one million dollar restriction was of any real significance. However, the constitutional limit has forced the Legislature to provide in the next budget for any deficits of the preceding period.

It is apparent therefore that if a balanced budget is desired and if section 4 of Article IX is changed by amending the present one million dollar limitation, a provision spelling out the requirement for a balanced budget might prove desirable. Any change in the language of this provision may require renewed court interpretation.

Notes to Chapter 3

1. Buck, Arthur E., *Public Budgeting*, 1929, pp. 3-4.
2. *Model State Constitution*, National Municipal League, 1963.
3. Pennsylvania Constitution, Article II, Section 1.
4. Pennsylvania Constitution, Article IV, Section 16.

ANNEX

*Testimony at Public Hearings
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*Statement of Philip P. Kalodner, Vice-Chairman and Chairman,
State Affairs Committee, Southeastern Pennsylvania Chapter
Americans for Democratic Action, before Taxation and
Finance Committee of the Preparatory Committee for
the Constitutional Convention*

TAXATION AND FINANCE COMMITTEE

The major policy question presented for the consideration of the Constitutional Convention in the area of state finance concerns the current one million dollar debt limitation.

Almost everyone who has studied the matter agrees that this debt limitation which has been honored in its breach by the utilization of Authority financing must be eliminated and that Pennsylvania should begin to finance its public projects with direct state debt.

The major question presented then is not whether the current limitation should or should not be removed—but what limitations if any should replace it. It is our view that the only limitations which should be imposed upon state borrowing are that it be “for a public purpose” and that the debt be limited in duration to the “useful life of the project” with some provision requiring some uniformity in the payment of the principal and interest during such project life.

We do not support the additional proposed limitation that any state debt be submitted and approved by the electorate. In our view the electorate is not in any better position to consider and determine the merits of such a matter than it is to consider and determine the merits of ordinary legislation. A Legislature which improvidently incurs debt can be effectively dealt with by the public refusing to elect its members. In fact Pennsylvania's experience has been that the lack of any effective debt limitation and the lack of the requirement of citizen approval has not resulted in the creation of excessive debt. For certainly the General State Authority is neither limited today by an absolute Constitutional requirement nor by any requirement for voter approval; and all that we are recommending is that the free borrowing power of the General State Authority limited as it is only by the legislative authorization, be conferred upon the state of Pennsylvania in its own name. To replace a provision incorporating an absolute debt limit with a provision requiring voter approval while at the same time permitting the continued utilization of Authority financing, would merely prevent the shift of borrowing

from the Authority to the state itself; for faced with the necessity of obtaining voter approval for direct financing, state government would merely continue to utilize the Authority vehicle and the entire purpose of the Constitutional change will be negated.

We also recommend that the Constitutional provisions with regard to state debt permit the creation by legislation of a system in which the state borrows in one bond issue for a number of local governments, merely aggregating their needs and then floating one bond issue to cover them. Although we do not think the Constitution should require such a system, we believe that it should clearly permit the utilization of such a system if authorized by the Legislature. Such a system with all public borrowing being accomplished in the name of the state through a limited number of bond issues each year would undoubtedly result in a substantial saving both in the cost of the floating of bond issues and in the interest rates to be paid to bond holders. The utilization of state credit for the benefit of local government would after all be merely a recognition of a fact of governmental life: that the state of Pennsylvania cannot permit a failure by any government deriving its authority from the state on any debt issue by such government.

With regard to the limitation on municipal debt which has recently been expanded, we believe that no limits should be constitutionally provided for three reasons. In the first place, concepts as to the amount of debt which is reasonable vary from time to time requiring a change in the limitations and the presentation of such a question of change to the public in the form of approval of a constitutional amendment almost inevitably leads to extraneous considerations becoming involved, as was demonstrated by the recent Philadelphia experience in connection with the school debt limitation. In the second place, a limitation tied to real estate valuation assumes an assessment which is uniform statewide as a percentage of market value; and, of course, the assumption is incorrect. Finally, and most significantly, a limitation tied to real estate valuation assumes that real estate will continue to be the major part of the municipal tax base or in the event that other taxes such as income taxes are utilized, that real estate, nevertheless, provides a correct measure of a community's ability to finance its own future. We reject both of these assumptions since we believe that increasingly local government will move away from a real estate tax base which is fundamentally regressive and inequitable and we believe that real estate value may become a less and less valid test of a community's resource particularly as apartment house construction replaces single family residential construction in the denser urban areas.

In our view, the constitution should merely provide that municipal governments shall be limited by the State Legislature with regard to the maximum amount of debt which they can borrow without voter approval and the maximum which they can borrow with voter approval. If all limitations are removed from the Constitution, then it will be unnecessary to make

provision with regard to the elimination from such limitations of any self-liquidating projects, although we do agree that in calculating any debt limitation imposed by the state the amount of such self-liquidating projects should be eliminated. Similar provisions to those already discussed in connection with state debt should be incorporated with regard to the public purpose of municipal debt, its limitation to the life of the improvement and the requirement that it be repaid on some fairly uniform basis over the life of the improvement which it is utilized to finance.

*Statement to the Pennsylvania Constitutional Convention
Preparatory Committee, Task Force Hearing on
Taxation and Finance, July 1967, by
The League of Women Voters of
Pennsylvania*

The League of Women Voters of Pennsylvania thanks the Preparatory Committee for this opportunity to present its views on that part of Article IX (Taxation and Finance) of the State Constitution which will be considered by the Constitutional Convention.

The League of Women Voters of Pennsylvania has almost 7,000 members in 56 local Leagues throughout the state. League members, over a period of 14 years, have studied many aspects of the State Constitution and our testimony today represents the conclusions and stands which have evolved from this study regarding state finance. We are not legislative draftsmen and have not, therefore, a draft in precise constitutional language of a Taxation and Finance Article, but would prefer instead to comment on the proposed draft presented by the Pennsylvania Bar Association.

In the light of our past study, we find that the Pennsylvania Bar Association draft of the Taxation and Finance Article makes several important and necessary changes in Article IX of the Constitution of 1874.

1. Their proposed draft removes the \$1 million debt limit, which in our day is unrealistic, has made State borrowing expensive and less responsive to the will of the people, and which contains a built-in inflexibility for the future.

a. Under the present provision, the State may borrow only up to \$1 million to supply current deficiencies in revenue unless the money is needed to repel invasion, suppress insurrection or defend the State in war. No provision is made in the State Constitution for borrowing for capital program except by constitutional amendment. Although \$1 million may have seemed a reasonable debt limit in 1873, when many present services were limited or non-existent and the total State budget was only \$7 million, it is no longer adequate by any standards. Lt. Governor Broderick, in an address this year to the delegates to the League of Women Voters State Convention presented this point graphically by explaining that limiting the State with its financial resources to a \$1 million debt is like limiting a man with a \$15,000 income to a debt of \$10.

b. The present government of Pennsylvania with greatly enlarged responsibilities for the welfare of its citizens, now serves over eleven million people. It must have the power to borrow money to provide the facilities it needs. Since it is denied such power, it has turned to the Authority device to build its schools, hospitals and other needed facilities. Except for its toll roads and bridges, with their revenue producing potential, this is a questionable way to finance government. It is more costly than straight government borrowing, since Authority bond interest charges are usually higher because the full faith and credit of the Commonwealth is not pledged. We are told that authorities pay from 1/2 of 1% to 1-1/2% more in interest than the State does. On a State authority indebtedness of at least \$1.5 billion, the additional interest paid every year can amount to from \$3,750,000 to \$22,500,000! Moreover, the Authority is not directly accountable to the people and Authority indebtedness can be increased by an act of the Legislature.

c. Constitutions need to be particularly flexible in regard to fiscal matters. Who can say what money value will be in 25 years or what new demands will be made on the state government? The League of Women Voters opposes any monetary debt limit.

2. The Pennsylvania Bar Association's draft proposals provide several procedural restraints on the State's borrowing capacity. Although the League of Women Voters opposes a monetary debt limit, we do consider desirable Constitutional provisions that encourage the State to meet its current obligations and to operate on a pay-as-you-go basis as nearly as possible.

We should like to point out that there are several procedures available to restrain the Legislature from fiscal irresponsibility. These could include:

- 1) Provision that a debt shall contain the means to pay principal and interest.
- 2) Provision for a sinking fund.
- 3) A requirement that bonds mature in a specified period.
- 4) Voter approval for the creation of new debt.
- 5) A requirement that new debt be created only by a 2/3 or 3/4 vote of the General Assembly.

Some of these proposals might be considered statutory and better left either to the legislature or to the money market. Too many restrictions on the power of the government to act in the field of state finance might lead to the perpetuation of unnecessarily costly authorities.

The proposals of the Bar Association include both a requirement that new debt be created by referendum and procedures for floating a bond issue. We should like to suggest that this might be overkill. Some of the detailed provisions could well be omitted from the Constitution in the interest of

producing a basic document uncluttered by legislative minutiae. We should today express more confidence than did the framers of the 1874 Constitution that our elected officials will conduct the financial affairs of the state in a responsible fashion.

To summarize, the League of Women Voters supports a change in Article IX of the Constitution of 1874 to eliminate the \$1 million debt limit and to substitute procedural restraints on the State's borrowing capacity. This change will increase the State's financial stability and provide flexibility for the future.

The League of Women Voters would also like to express the hope that the Preparatory Committee will recommend to the Constitutional Convention that the Convention itself or Convention committees hold public hearings on the four constitutional topics assigned by the voters to the Convention for consideration. We suggest that the more citizen involvement there is in the deliberations of the Convention the more the voters of the Commonwealth will feel that the Constitution is truly their document and one deserving their close attention and support.

*Statement on the Provisions on Taxation and State Finance in the
Pennsylvania Constitution, by A Modern Constitution for
Pennsylvania, Incorporated, Harrisburg, Pennsylvania,
July 20, 1967*

To the Members of the Preparatory Committee for the Pennsylvania Constitutional Convention of 1967

Gentlemen:

Most of the members of this panel with whom we have had some prior contact are aware of some of the difficulties under which our organization, A Modern Constitution for Pennsylvania, Inc., must act. We are a non-profit, tax-exempt, voluntary citizen organization devoted to research and the dissemination of information on revision of Pennsylvania's Constitution of 1874, and are prohibited from making efforts to influence the enactment or defeat of any legislation.

As such, we must avoid the temptation to solve the fiscal problems of the Commonwealth for the next hundred years or so with any plan of our own.

But there is no reason why we cannot or should not express our great approval of a proposal that has just been offered to you on behalf of the Pennsylvania Bar Association for the much needed modernization of Article IX of the Constitution of 1874—or at least that major portion of Article IX with which the Convention will be authorized to deal.

By far the most important provision in this remarkably lucid and brief proposal is the one to permit the creation of debt by the Commonwealth for any purpose whatsoever, as long as it is approved by a majority vote in a statewide referendum.

There has long been general agreement on the need to eliminate the archaic prohibition against any state debt, except for casual deficiencies never exceeding \$1 million at any one time. The restriction had its origins 125 years ago, during the aftermath of the 1837 Depression, when Pennsylvania was one of a group of 9 states that defaulted on bonds which they had sold to finance the construction of railroads and canals.

This occurred too late to prompt the drafting of any restriction on state debt in the Constitution of 1838, but in 1857 an entire article on state debt was added by amendment, one section of which prohibited the state from incurring any debt whatsoever in the future, except for purposes of defense. Here, then, is the precedent for the restriction that has made it constitu-

tionally impossible for the Commonwealth to finance its capital development for more than a century.

Until a way was found to circumvent this restriction—which, incidentally, was also adopted by many other states for similar reasons at the same critical time in our history—the costs to the Commonwealth in terms of arrested development were high.

And, when the way was found, the cost of meeting the increased interest requirements that inevitably accompanies the marketing of public bonds which are not guaranteed by the full faith and credit of the public has been great.

Dr. A. James Heins of the University of Illinois has recently explored the cost of borrowing by revenue bonds, such as are issued by our Pennsylvania public authorities, and by general obligation bonds, such as are issued by states with debt capability.

Taking the period from July, 1956, through December, 1959, as a base, he computes the probable difference in annual interest paid on revenue bonds issued by Pennsylvania and six other states, and the probable interest that would have been paid on general obligation bonds for the same amounts and terms, and marketed at the same time. He then projects this difference over the life of the issues.

Pennsylvania comes out comparatively well. On bonds of \$188.4 million, our excess cost was only \$8.9 million. Indiana's excess cost was almost the same on borrowings of only \$50.4 million. Illinois bonds totalled less than half of ours, with more than four times the excess interest cost.

Whether one accepts Dr. Heins' figures as absolute, two facts emerge:

1. Pennsylvania's fiscal management has been relatively astute.
2. Pennsylvania's fiscal management has been constitutionally handicapped.

The dangers of writing restrictions into a constitution are well documented. Giving the General Assembly the right to borrow unlimited amounts for any necessary purpose, as long as the amount and purpose has been approved by the voters, is a system happily used by about half the states, in varying forms. It is the basis of the Pennsylvania Bar Association proposal. It is one which A Modern Constitution for Pennsylvania, Inc., has studied and endorsed.

Without in any way retreating from our endorsement of this proposal, we would like to take this opportunity to call to your attention another proposal, also one which had the Pennsylvania Bar Association approval 13 months ago, but which was then tabled for further study. While this is a simple concept and commonly in use in the private sector, it is, we believe, new and perhaps even unique in its application to government.

It is based on the premise that an individual, business, or government can incur debt safely only up to his or its demonstrated ability to repay.

This was drafted into amendment form last year by a group of distinguished attorneys, including former Attorney-General David Stahl of Pittsburgh, Nathan B. Feinstein, Esq., Philadelphia, and others. In this statement we shall refer to their work as the Stahl-Feinstein amendment.

They were responding to a complaint by then candidate for Governor, Milton J. Shapp, that the hazards of submitting proposed bond issues to a statewide referendum are often too great. The cost of money may increase during the waiting period which is rarely less than one year, reducing the issue's net yield. Nothing gets done about the purposes for which the money is needed during this period, and problems frequently multiply so that more money is needed by the time the bonds can be issued than had originally been planned and approved. The greatest danger of all in this procedure, however, is to hold up an essential program for a year or more, waiting for funds, and then to have it rejected by an uninformed or unaware electorate, all too often the result of lobbying by well financed pressure groups.

They proposed that the General Assembly be given the right to incur debt, as long as the principal and interest on the debt is safely within limits of the Commonwealth's ability to pay.

They proposed to set these limits the same way you and I determine them for ourselves and our businesses—by conservatively estimating our future income and the portion of it that we can spare after making allowance for other fixed expenses.

They proposed that an average of the Commonwealth's uncommitted General Fund revenues over the past five years should be the base on which to compute these limits.

They proposed that 10% of this base could be used for debt service with safety and propriety.

On this basis, they drafted an amendment to Article IX which was submitted to—and approved by—the Project Constitution Committee during the 1966 summer meeting of the Pennsylvania Bar Association.

However, when it was submitted to a larger group of Bar Association members, many questions were raised about what effect it would have if it should ultimately be approved as an amendment to the Constitution. Unfortunately, the brief time in which the proposal had been conceived and drafted had not permitted any economic studies, so no one had useful answers.

As a result, the proposal was withdrawn, and the Bar Association went on record as supporting the same Taxation and State Finance amendment they had supported previously, and substantially the same amendment they have put before you today.

A Modern Constitution for Pennsylvania, Inc., had previously studied this proposal and approved it. Nevertheless, we found the Stahl-Feinstein concept sufficiently original and progressive that we undertook a quiet investigation of its potential.

We found no reason to disagree with Judge Robert E. Woodside's contention that the proposal, as it was then worded, would give the General Assembly and the governor in office at the time it became effective a "blank check." However, we found nothing to substantiate his estimate of the size of that check as "billions of dollars."

The General Fund Revenues for five fiscal years ending 1967 average \$662.3 million. When the \$60 million in annual commitments to the General State Authority and to Project 70 bond holders is deducted, the average uncommitted General Fund Revenues are about \$600 million.

The 10% formula would allow a maximum of \$60 million for debt service. We consulted economists, bankers and securities experts to learn how much the Commonwealth could borrow with this. We were told that, at prevailing rates, it should be between \$818 million and \$984 million.

This estimate corresponded with national averages on state debt and state revenues.

As to the "blank check" criticism, one broker pointed out that the market for bonds, despite higher interest rates, is not unlimited. He doubted that any excessive issues could be placed, regardless of interest.

At any rate, it would not seem too difficult to provide new language for at least this part of the proposal, to safeguard against the Governor or General Assembly ever utilizing more than a certain percentage of the state's total debt capacity under this proposal in a single year.

While we do not endorse this Stahl-Feinstein proposal, we find it meets the standards of prudent financial management as well as the demands of good government.

It is something of an innovation, but so was most of the Federal Constitution when it was first written.

It gives the General Assembly and the Governor the right and responsibility of deciding how much debt to incur, and for what.

It permits the State to borrow without delay in the event of emergency.

It relates state debt to state revenues, and to the general economy.

We urge the study of these provisions by the Preparatory Committee and by the Constitutional Convention.

Meanwhile, let us repeat—A Modern Constitution for Pennsylvania, Inc., is pleased to endorse and support the Pennsylvania Bar Association proposal which corrects the restrictions of Article IX of the Constitution of 1874, and which provides a way of financing the Commonwealth's future needs in a way that has been used successfully by more than 20 other states.

A Modern Constitution for Pennsylvania, Inc.

Richard C. Bond, President

Robert Sidman, Executive Director

*The Pennsylvania AFL-CIO Position on Taxation, presented by
Harry Boyer, President, before The Preparatory Committee
for the Commonwealth of Pennsylvania
Constitutional Convention*

That the Commonwealth is plagued by acute problems in its effort to solve fiscal needs of the state is attested to by the agonizing and torturous bind in which the General Assembly currently finds itself.

There is no question but that this dilemma will recur every time it becomes necessary to budget for the proper needs of the Commonwealth and its citizens.

Part of the dilemma is that the Governor and the General Assembly interpret too rigidly and too narrowly existing limitations found in the Constitution. The result of such a narrow view is that we have arbitrarily limited and confined the sources of such taxes, with each individual class of citizens protesting it should not be singled out.

Another result of such a narrow view is that exemptions of classes of citizens and enterprises are established, further limiting the availability of tax sources.

The consequences of such a practice is truly a painful one for Pennsylvania. While we increase taxes in a helter-skelter crazy-quilt fashion, we actually have not been improving our situation when Pennsylvania is compared to the rest of the country.

For example, in 1961 the national average state per capita revenue was \$157.49. Pennsylvania ranked 40th among all the states with a per capita general revenue of \$140.18, lagging behind the national average by \$17.31. In 1965 the national average state per capita revenue was \$212.05. Pennsylvania, lagging 41st among all states had a per capita general revenue of \$187.25, lagging behind the national average by \$24.80.

The relationship between per capita tax revenue and the functions and services provided by the state is an undeniably close one. Thus, in 1965, when we ranked 41st among the states in per capita tax revenue, we ranked 40th among the states in terms of per capita state general expenditures.

In state support for public education, we were 36th; in state aid to higher education we were 49th; in state support for highway construction we were 44th; in state support for hospitals we were 41st; in daily expenditures for patients in our state mental hospitals we were 34th; and in terms of the number of doctors per hundred patients in these hospitals we were 43rd.

It is clear that while Pennsylvania has been struggling to improve those conditions, we are not equaling progress made in other states, and, in fact, are dropping further behind.

Bold, vigorous steps must be taken by the Constitutional Convention to make possible the administration's goal of excellence at the best, or a decline in our standing among the states at the worst. One such approach is to examine the area of exemptions from taxes. The Pennsylvania AFL-CIO believes that the exemptions now accorded to religious and other non-profit organizations and institutions is not only unwarranted but unfair to the citizens as a whole. The entire scope of such exemptions should be re-examined and evaluated by the Constitutional Convention. We emphatically hold that income-producing properties owned by religious and non-profit organizations such as educational institutions, hospitals, etc., not related to the actual purposes for which the institution or religious organization is established, should certainly not be free of responsibility under state and local tax programs.

There is a growing concern nationally that such freedom from taxes for all of the properties, whether they are related to the essential purpose or not, does, in fact, constitute social inequity.

At the least, income-producing property not related to the essential purposes should at once be made subject to state and local tax laws. Additionally, there is no reason why public utilities should enjoy freedom from any taxes which other enterprises must pay. While essentially public utilities are free of property taxes—a matter of local concern—the increase in such local revenues would place to that degree a lesser burden upon the Commonwealth to subsidize essential services at the community and county level.

We believe that this entire subject matter is appropriate for consideration by the Constitutional Convention, for a constitutional requirement is less apt to be subject to capricious change by either local or state legislative bodies.

The Pennsylvania AFL-CIO would, of course, prefer that any existing bar to a graduated income tax be altered to permit same. In our considered judgment this represents the only viable manner through which our fiscal difficulties can be solved. We are aware of the fact that the referendum authorizing the Constitutional Convention contains certain restrictions. Whether or not such restrictions are binding upon a Constitutional Convention has been open to serious challenge by some who are learned in the law. We earnestly hope that the Constitutional Convention will endeavor to resolve this toward the end that an orderly and effective manner of raising tax revenues may be contemplated and set into motion.

*Proposal of the Pennsylvania Bar Association Relative to
Taxation and State Finance, Submitted to the
Preparatory Committee for the
Constitutional Convention*

Section 1. *Uniform Taxation; Exemption from Taxation*—All taxes shall be uniform, upon the same class of subjects, within the territorial limits of the authority levying the tax, and shall be levied and collected under general laws; but the General Assembly may, by general laws, exempt from taxation public property used for public purposes, actual places of religious worship, places of burial not used or held for private or corporate profit, institutions of purely public charity and real and personal property owned, occupied, and used by any branch, post, or camp of honorably discharged soldiers, sailors, and marines; and the General Assembly may, by general laws, set up standards and qualifications for private forest reserves, and make special provision for the taxation thereof. Citizens and residents of this Commonwealth, who served in any war or armed conflict in which the United States was engaged and were honorably discharged or released under honorable circumstances from active service, shall be exempt from the payment of all real property taxes upon the residence occupied by the said citizens and residents of this Commonwealth imposed by the Commonwealth of Pennsylvania or any of its political subdivisions if, as a result of military service, they are blind, paraplegic or double or quadruple amputees, and if the State Veterans' Commission determines that such persons are in need of the tax exemptions granted herein. Any taxing authority may exempt from occupational privilege taxes, persons deriving less than one thousand dollars per year from such occupation.

(Constitution of 1874, Article IX, Section 1, as Amended, November 2, 1965)

Section 2. *Exemptions to Residents of Other States*—Taxation laws may grant exemptions or rebates to residents, or estates of residents, of other States which grant similar exemptions or rebates to residents, or estates of residents, of Pennsylvania.

(Constitution of 1874, Article IX, Section 1B, as Amended, November 6, 1928)

Section 3. *Exemption from Taxation Limited*—All laws exempting property from taxation, other than the property above enumerated shall be void.

(Constitution of 1874, Article IX, Section 2)

Section 4. *Taxation of Corporations*—The power to tax corporations and corporate property shall not be surrendered or suspended by any contract or grant to which the State shall be a party.

(Constitution of 1874, Article IX, Section 3)

Section 5. *State Debt*—(a) Except as hereafter in this article provided, no debt shall be created by this Commonwealth unless:

(1) The debt has been authorized by statute, and

(2) It is incurred to suppress insurrection, to rehabilitate areas affected by disaster, by the issuance of tax anticipation notes payable in the fiscal period in which they are issued, or to implement authority voted by the electors prior to the adoption of this article for the acquisition of land for State parks, reservoirs, and other conservation, recreational and historical preservation purposes, or for a Land and Water Conservation and Reclamation Fund to be used for the conservation and reclamation of land and water resources of the Commonwealth, including the elimination of acid mine drainage, sewage, and other pollution from the streams of the Commonwealth, the provision of State financial assistance to political subdivisions and municipal authorities of the Commonwealth for the construction of sewage treatment plants, the restoration of abandoned strip-mined areas, the control and extinguishment of surface and underground mine fires, the alleviation and prevention of subsidence resulting from mining operations, and the acquisition of additional lands and the reclamation and development of park and recreational lands previously acquired, or

(3) The debt is for other purposes separately specified in the statute and the question whether the debt shall be incurred has been submitted to the electors after such advertising as the General Assembly shall require and a majority of those voting on the question shall have voted in the affirmative.

(b) The General Assembly may authorize by statute the issuance of general obligation bonds or notes for the purpose of assuming or refunding any debt issued by any Commonwealth authority and which is payable or may hereafter become payable from Commonwealth revenues under leases to this Commonwealth, and it may from time to time authorize by law the issuance of refunding bonds or notes to pay any direct debt of the Commonwealth.

(c) All debt of the Commonwealth shall be evidenced by its general obligation bonds or notes which, except for tax anticipation notes, shall be bonds with serial maturities or notes repayable in installments over a period of time which shall be provided by law. The first serial maturity of bonds or the first payment of principal of notes of each issue of bonds or notes shall be not more than two years after the date of issue.

(d) All bonds or notes issued by the Commonwealth for capital improvements shall mature within a period not to exceed the estimated usefulness of the property or improvement for which they are issued and revenue shall be provided to pay the interest and retire the principal of such bonds or notes

within this period. The estimated period of usefulness shall be stated in the statute authorizing the project, and when so stated shall be conclusive.

(Pennsylvania Bar Association)

Section 6. *Limitation on State Loans*—All laws, authorizing the borrowing of money by and on behalf of the State, shall specify the purpose for which the money is to be used, and the money so borrowed shall be used for the purpose specified and no other.

(Constitution of 1874, Article IX, Section 5)

Section 7. *Municipal or Private Debt not to be Assumed by State*—The Commonwealth shall not assume the debt, or any part thereof, of any city, county, borough, township or other political subdivision, or of any individual, association or corporation, unless such debt shall have been contracted to enable the State to suppress insurrection or defend itself in time of war.

(Pennsylvania Bar Association)

Section 8. *State Sinking Fund*—(a) To provide for the payment of the present Commonwealth debt, and any additional debt contracted, the General Assembly shall continue to maintain a sinking fund, sufficient to pay the principal of and interest on the debt. If at any time the General Assembly fails to make an appropriation for this purpose the State Treasurer, any other provision of this Constitution notwithstanding, shall set apart from the first revenues thereafter received applicable to the appropriate fund a sum sufficient to pay the interest installments of principal or contributions to the sinking fund and shall so apply the moneys so set apart. The State Treasurer may be required to set aside and apply such revenues at the suit of any holder of Commonwealth bonds.

(b) No part of the sinking fund shall be used or applied otherwise than in the extinguishment of the public debt until all bonded debt of the Commonwealth has been completely repaid. Any money remaining in the sinking fund at such time shall be transferred to the appropriate fund and may be apportioned by the General Assembly.

(Pennsylvania Bar Association)

Section 9. *Surplus Funds*—The moneys of the State, over and above the necessary reserve, shall be used in the payment of the debt of the State, either directly or through the sinking fund, and the moneys of the sinking fund shall never be invested in or loaned upon the security of anything, except the obligations of the United States or of this State.

(Pennsylvania Bar Association)

Section 10. *Punishment for misuse of State moneys*—The making of profit out of the public moneys or using the same for any purpose not authorized by law by any officer of the State, or member or officer of the General Assembly, shall be a misdemeanor and shall be punished as may be pro-

vided by law, but part of such punishment shall be disqualification to hold office for a period of not less than five years.

(Constitution of 1874, Article IX, Section 14)

Section 11. *Gasoline, motor fuel, excise, motor vehicle registration, etc., taxes; appropriation and use*—All proceeds from gasoline and other motor fuel excise taxes, motor vehicle registration fees and license taxes, operators' license fees and other excise taxes imposed on products used in motor transportation after providing therefrom for

(a) Cost of administration and collection,

(b) Payment of obligations incurred in the construction and reconstruction of public highways and bridges shall be appropriated by the General Assembly to agencies of the State or political subdivisions thereof; and used solely for construction, reconstruction, maintenance and repair of and safety on public highways and bridges and air navigation facilities and costs and expenses incident thereto, and for the payment of obligations incurred for such purposes, and shall not be diverted by transfer or otherwise to any other purpose, except that loans may be made by the State from the proceeds of such taxes and fees for a single period not exceeding eight months, but no such loan shall be made within the period of one year from any preceding loan, and every loan made in any fiscal year shall be repayable within one month after the beginning of the next fiscal year.

(Constitution of 1874, Article IX, Section 18)

REPEALER

Sections four, five, seven, eight, ten, thirteen, fifteen, two sections numbered sixteen, seventeen, nineteen, twenty-one, twenty-two, and twenty-three of Article IX of the Constitution of 1874 are hereby repealed effective immediately.

Sections twenty-four and twenty-five of Article IX of the Constitution of 1874 are hereby repealed effective when the last bonds or notes have been issued under their authority.

*Statement of William A. Schnader on Taxation and State
Finance before the Preparatory Committee for the
Pennsylvania Constitutional Convention*

Act No. 2 of 1967, under which the Constitutional Convention will be functioning, specifically prohibits it from recommending the modification of the uniformity clause in Article IX of the Constitution of 1874 or of Section 18 of the same Article.

The former prohibition will prevent the convention from recommending to the people that the Legislature be given power to enact a graduated tax of any kind. The second prohibition will prevent any recommendation for a change of that section of the Constitution which creates the Motor License Fund.

The State's borrowing power is covered by Article IX, Section 4 of the Constitution of 1874, as last amended on November 6, 1923. This section as it stands has undoubtedly cost the taxpayers of Pennsylvania many millions of dollars.

During the past 93 years, with certain exceptions for which the Legislature has never borrowed money, the only way that an indebtedness of more than one million dollars could be incurred was by amending the Constitution. However, more than a billion dollars has been borrowed under constitutional amendments for highway purposes, to pay soldiers' bonuses, to acquire and free toll bridges throughout the State and most recently for conservation purposes. Constitutional amendments could be made only as provided by old Article XVIII which required at least two or three years for adoption by two Legislatures and by the people at the polls.

However, in 1935, someone conceived the idea of creating so-called authorities to which the Legislature might give the power to borrow money and which would then erect buildings or construct roads and bridges, entering into leases with the Commonwealth to pay rentals for the use of whatever facility had been erected, at rates which would cover interest and amortization of principal, thus extinguishing the debt in a certain number of years. This device was sustained as constitutional by our Supreme Court and through it the Commonwealth has borrowed billions of dollars indirectly as have also the various political subdivisions of the State.

The Commonwealth itself can command a lower interest rate than any of these authorities and by the use of authorities there cannot help but be a duplication of personnel attending to work which could be done without duplication.

Among the 50 states the constitutional provisions relating to the borrowing of money differs widely. The proposal which the Pennsylvania Bar Association is offering to you as an Article on Taxation and State Finance cannot be said to have any prototype in the constitution of any other state.

The Woodside Commission originally recommended that Article IX, Section 4 of the Constitution be amended by giving the Legislature the power with the approval of the voters to borrow money for capital improvements. It would have banned authorities completely.

The Bar Association proposed a different version, the Scranton Commission a still different one and the present version is a rewrite by the Bar Association. It permits the Legislature without a vote of the people to borrow money to suppress insurrection, to rehabilitate areas affected by disaster, and to implement the two most recently adopted amendments authorizing the borrowing of \$70,000,000 and \$500,000,000, respectively, for conservation purposes. It would also expressly approve the issuance of tax anticipation notes payable in the fiscal period in which they are issued.

With the consent of the voters the Legislature could borrow money in any amount for any other purpose.

I have been informed that in the 1966 Session of the Legislature there was a group which desired to give the Legislature the power without a vote of the people, to incur indebtedness far beyond that which our proposal would permit.

It seems to the Bar Association that with the exceptions named in our proposals the Legislature should not be permitted to incur any indebtedness for any purpose without the approval of the voters. We believe that this is sound government and should be adhered to in revamping this very important section of the Constitution.

We are not proposing that authorities be prohibited.

We would leave it to the good conscience of the Legislature to decide in each instance whether money could be borrowed more cheaply and used more efficiently through the regular channels of government or by an authority.

We are recommending the modification of what are Sections 9, 11 and 12 of the present Constitution relating, respectively, to the prohibition of the assumption of municipal or private debt by the Commonwealth, the State Sinking Fund, and surplus funds. We believe that a mere reading of these provisions will satisfy you that our proposals are improvements over the text of these sections as they stand at present.

We are also suggesting the repeal of Sections 4, 5, 13, 15, two Sections 16, 17, 19, 21, 22 and 23 of the present Constitution as completely obsolete. We also suggest the repeal of the recently adopted "Project 70" amendment and the amendment authorizing a \$500,000,000 bond issue for conservation purposes, effective when the last bonds have been issued under these respective amendments. Once the money has been borrowed under amendments

such as these, there is certainly no reason for having them clutter our Constitution.

We would preserve without change Sections 1, 1(B) (renumbered 2) 2, (renumbered 3) 3, (renumbered 4) 6, 14 and 18 of Article IX and we would transfer to the Article on Local Government, Sections 7 and 10 of the present Article IX. These last mentioned sections deal with municipal finance rather than with state finance.

*Text of Testimony before the Constitutional Convention
Task Force on Taxation and Finance, Offered by
Pennsylvania Home Builders Association*

My name is Herbert M. Packer, Jr., Executive Vice President of the Pennsylvania Home Builders Association, a state-wide trade association representing 2,500 members in the residential construction industry.

With me is J. Scott Calkins of the Harrisburg law firm of Shaffer, Calkins & Balaban, Legal Counsel to our Association.

To offer brief background information on our organization, gentlemen, we represent Local Home Builders Associations in the following metropolitan areas of the state:

Allentown-Bethlehem-Easton; Wilkes Barre-Scranton-Hazleton; Chambersburg; Gettysburg; York; Lancaster; Harrisburg; Reading; State College; Sunbury-Selinsgrove-Lewisburg; Altoona; Johnstown-Somerset-Indiana; Washington; Uniontown; Erie; Williamsport; Pittsburgh, and Philadelphia.

We have asked to testify because of our concern for effective tax reform within the Commonwealth so desperately needed to insure both a sound tax base for state and local governments and an equitable tax burden upon our citizens.

Without such equity, other benefits of home ownership may well shrink in contrast before excessive and unrealistic real property taxes.

Broadly defined, the subjects within the field of taxation and finance with which we are concerned are: 1) Tax exemption policies; 2) Tax incentives, abatement and postponement; 3) broad based taxes; and 4) tax assessment policies which directly affect the rate and amount of taxes paid by our citizens.

TAX EXEMPTION POLICIES

Many responsible organizations have voiced their concern, which we share, at the growing list of tax-exempt properties throughout our Commonwealth. The Chief Assessor of the City of Johnstown recently had some illuminating remarks to make on this subject.

It requires no fiscal genius to recognize that each new tax-exempt property places the burden of taxation more heavily on those properties remaining on the tax rolls.

It might be slightly more difficult to realize that lack of a stringent Constitutional and Legislative policy on tax exemption can and probably will

cost Pennsylvanians badly needed governmental services at the state and local level simply because increasing taxes on taxable properties will, at some point, no longer be tolerated by the taxpayers. At that point, which most assuredly will come, governments will be short the additional dollars required for such services.

Rest assured, we take no exception to justifiable tax exemptions such as those granted to houses of worship.

We do, however, vigorously oppose and hope to see the Constitutional Convention take steps against those tax exemptions granted to church-owned commercial and industrial properties, educational and charitable business-related activities, and other non-profit corporate activities in unfair but privileged competition with business and industry.

We also recommend that the delegates to our Constitutional Convention take a long, hard look at tax exemptions granted to many of those companies under the regulation and control of the Public Utility Commission.

Another problem facing state and local governments in the field of tax exemptions is the growing clamor in certain circles to exempt persons over 65 years of age from payment of real property taxes, and taxes on wages and income. We urge the delegates to the Constitutional Convention to avoid the temptation of relegating our elderly to the role of second class citizens. We do not oppose aid for those elderly who desperately need it. We do, however, strongly oppose saddling younger citizens with increased real property and wage and/or income taxes for no other reason than potential political favoritism of the elderly!

Finally, we earnestly hope that delegates to the Constitutional Convention will act to solve the recurring problem of payments in lieu of taxes ordinarily due local government from state and/or federally owned properties within its boundaries. I am certain that you are all aware of the unfair economic burden placed upon local government resulting from loss of such needed taxes.

TAX INCENTIVES, ETC.

In the second category, tax incentives, abatement, and postponement, it has long been our belief that an intelligently applied policy, spelled out in our Constitution, would be of tremendous value insofar as tax revenue is concerned. Think of the many cases which have wended their weary way through our courts dealing with tax incentives, tax abatement and tax postponements. One vitally affecting our industry is now before our State Supreme Court. Its contestability, as far as plaintiff and defendant were concerned, lay in the uniformity clause of our present Constitution, the use of which has, we believe, been extended far beyond what the framers and those who added to our Constitution had intended. Let me state, quickly, that we recognize that the Constitutional Convention cannot touch or alter the uniformity clause but it is our belief that the philosophy of tax in-

centives, abatement and postponement can be constitutionally granted without changing the uniformity clause.

What, you may ask, are tax incentives, tax abatement and tax postponement? There are numerous examples of each. A tax incentive plan is currently before the General Assembly. It would grant tax credit to industry and business for investment in equipment to control air and water pollution. Tax abatement means lessening or doing away with certain taxes when in the interest of encouraging industrial or residential development, etc. There has been little or no tax abatement in Pennsylvania because of the constitutional-legal question. Tax postponement is more frequently found. The General Assembly has enacted several tax postponement measures, chief among which is the 1963 amendments to the interim reassessment laws granting temporary relief from increased assessments as a means of stimulating the sale of residential dwelling units.

Our industry has learned that, in certain instances, tax incentives, abatement, postponement, or a combination of all three, can stimulate construction and sale of housing.

Yet, for many reasons including economics, shortage of tax revenues, etc., many if not all tax relief measures have faced legal challenge. To be even more specific, it is quite possible that relief from the state realty transfer tax—which represents double taxation at its worst since a five percent sales and use tax is paid on all materials used in construction, on top of which is added this one percent additional “sales” tax—could be successfully challenged in court under our present Constitution. This despite the fact that the yield from realty transfer taxes on residential construction has been dropping; despite the fact that tax experts agree that realty transfer taxes are regressive in nature; despite the fact that such a tax incentive could dramatically stimulate construction of desperately needed new housing units in Pennsylvania; and despite the fact that construction of more new housing units will result in an average sales and use tax yield of \$475 per unit!

We have no specific language to suggest insofar as how incentives, abatement and postponement could be made permissible constitutionally. We leave this to persons more competent than we. Our plea is only that attention be given to this problem and solutions found if our case is justified.

BROAD BASED TAXES

The next category is, perhaps, the most sensitive subject in the history of our Commonwealth, broad based taxes.

We believe, however, that no matter how touchy this subject may be, Pennsylvanians owe it to themselves to discuss openly and candidly sales and use taxes, income taxes and the like, unpleasant but demanding forms of revenue. Not to do so would be to cheat ourselves.

Since this testimony is “on the record,” we may just as well seize the pro-

verbal "bull by the horns" and state categorically that our new, revised Constitution must clearly permit some kind of state income tax. What kind is not within our province to say. The fact, however, that one is needed is irrefutable and within our province to state.

Proposed alternative taxes such as those the effect of which could be to dry up mortgage and construction money, weaken the already dim profit picture of member firms within our industry, or make home ownership even more undesirable, can only cause irreparable harm to our industry and to the citizens of our Commonwealth.

Let's face the facts, gentlemen! Taxes on property are rigidly set obligations. If our economy staggers, such taxes are usually the last to drop. On the other hand, sales and use taxes and income taxes are fluid in that they are based, essentially, on the amount earned or the amount spent. In times of economic difficulty, you automatically pay less on what you earn, and you pay less because you spend less!

We have one final comment to offer on the desirability of broad based taxes. There is no question in the minds of builders that we have come dangerously close to the saturation point insofar as real property taxes are concerned. Add to this the miserable fact that we are hounded by hundreds of nuisance taxes dotting the books to harass home owner, renter, buyer, wage earner, amusement seeker, drinker, sportsman, etc.

Where will our governments turn to get the additional tax revenue we're told must be raised to provide the services we're told we demand?

There is only one other source, and we all know what it is!

Let's "screw up our courage to the sticking point" and do what we must do... NOW!

TAX ASSESSMENT POLICIES

Policies affecting assessment of real estate for tax purposes are, perhaps, of greatest concern to the housing industry principally because of capricious and arbitrary decisions, confusion, and lack of a single, definite policy throughout our 67 counties.

Take the case of raw, undeveloped land. In one county, it lies reasonably taxed for a stated period of time even though subdivision plans have been prepared for future development. When that stated period of time has elapsed, whether developed or not, the assessment is gradually and properly raised. County officials enthusiastically supported this theory recognizing what such a stimulant could do for the county, its political subdivisions, our industry, and the citizens.

In the county next door, all that the Board of Assessment needs is a vague rumor that a certain farmer intends to sell his ground for use as a housing development and the assessment will rise as quickly as the law will permit.

In yet another county, a high rise multifamily unit was reassessed floor by floor as it was constructed, so desperate for revenue were the two taxing bodies. Yet, not one dollar had been earned from rentals by the developer.

Such widespread variance in assessment practices graphically demonstrate the inconsistencies we decry.

The tragedy of such assessment practices is that the assessment should be utilized as a stimulant to our economy as well as the means through which tax revenues are obtained. A sound multifamily unit, successfully constructed, is worth far more in terms of tax revenue than the comparatively few dollars obtained from interim reassessment. Furthermore, housing is the only major commodity on which taxes are levied and collected *before* sale.

CONCLUSION

This completes our testimony which, we hope, has been informative, useful and within those sensible limitations set by the Preparatory Committee. We earnestly hope that the Committee and the delegates themselves will give serious consideration to our views and our proposals.

We sincerely believe that these proposals are in the best interests of all of the citizens of our Commonwealth, both individual and corporate.

It remains only for me to thank you, gentlemen, for the privilege of presenting the views and recommendations of our Association.

If you have any questions, I will be happy to attempt to answer them.

Thank you.

Statement of Pennsylvania Municipal Authorities Association for Preparatory Committee for the Constitutional Convention

The position of the Pennsylvania Municipal Authorities Association, stated in broad general terms, is that the Constitution should be written in a manner to make available to the citizens of this Commonwealth a free choice as to the method of creation, operation, and financing of their proprietary functions.

The Pennsylvania Municipal Authorities Association submits the following language as language to replace the present Article IX, Section 8 of the Constitution, the last amendment of which was in 1966 by the electorate:

Municipal Debt.—(a) The debt of any county, city, borough, township, school district, or other municipality or incorporated district, shall never exceed fifteen per cent upon the assessed value of the taxable property therein, nor shall any such county, municipality or district incur any debt, or increase its indebtedness to an amount exceeding five per cent upon such assessed valuation of property without the consent of the electors thereof at a public election in such manner as shall be provided by law.

(b) Obligations payable solely from the net operating revenues from designated projects are not debt within the meaning of this section.

The Pennsylvania Municipal Authorities Association recommends the retention of the limitation of 15% and 5% as the same was approved by the electorate in 1966 and represents the recent thinking of the population. As persons vitally interested in public debts, all of the members of the governing board of the Authorities Association recognize that a reasonable limitation on debt is a requisite to efficient operation of government on any level. As the Legislature and the electorate have recently expressed themselves, this Association does not propose any change in the approved percentages. A uniform debt limitation is proposed for all political subdivisions.

The new subsection (b) proposed makes clear that the Authorities Association feels that municipalities should have the right, if they desire, to issue non-debt revenue bonds. The projects thus financed are self-sustaining and self-liquidating. Subsection (b) would not prohibit the formation of Authorities. However, the desirability of the formation of an Authority as a means of acquiring, operating and discharging the obligations which are imposed by the acquisition of projects would be left to the governing body of the municipality. Thus, the American freedom of choice, of which we are all so proud, would remain an integral part of the operation of municipalities.

This would be true not only of the financing of projects but also in operation as will be pointed out subsequently in this statement.

A brief review of the background of Authorities is necessary to clarify this position and make clear why the Authorities Association feels that the Authority method of operating municipal projects should not be abolished.

Authorities are relatively new in Pennsylvania. The first general act was enacted in 1935. Between 1935 and 1945, only 76 Authorities were incorporated. As of December 31, 1965, there were incorporated 1769 Authorities operating 265 water projects, 312 sewer projects and 762 school projects. The following summary shows the investment of private, municipal and water Authority operations.

Gross Investment	Private \$383,156,000	Municipal \$436,579,000	Authority \$430,133,000
Water sold M.G.			
Metered	122,691	168,957	95,618
Unmetered	<u>21,542</u>	<u>13,648</u>	<u>15,429</u>
Total	144,233	182,605	111,047
Total Revenues for Metered and Unmetered Water	\$52,103,000	\$42,311,000	\$44,164,000

The high investment for 1,000 gallons of water sold shows that the Authorities are serving where private capital will not invest or municipal operations cannot be made available. The following summary shows the pertinent statistics for sewer Authorities:

Gross Investment	\$547,237,000
Operating Revenues	48,016,000
Number of Customers	1,111,041

There are three main reasons for the operation of Authorities. The first is a jurisdictional one. The first Authority in the United States was the New York Port Authority. It was created to serve the State of New York and the State of New Jersey. Many Authorities in Pennsylvania serve from two to twenty municipalities by one operation.

The second reason for the formation of Authorities is the conducting of the proprietary field of government in accordance with sound business practices. An Authority can offer long term employment in various projects, particularly in the water and sewer field, without the question of possible loss of jobs at any ensuing election. They are also able to offer training courses for their employees. The Pennsylvania Municipal Authorities Association conducts conferences several times a year to educate and train men and employees in Authority operations. It also has an annual conference where information is given and traded in regard to the operation of various projects operated by the members of the Association.

The third reason for the creation of Authorities is financial. Under the Constitution as now amended, borrowing power has been increased to 5% and 15%, as opposed to the former 2% and 7%. As stated above, the Association makes no recommendation for a change in this as it will be noted that there is included a paragraph (b) to make possible the issuance of non-debt revenue bonds which would not be counted against the debt limitations of a municipality.

Many questions have been raised regarding the appointment of board members of Authorities, rather than election. The Pennsylvania Municipal Authorities Association recently made a survey that concerned board members, and out of 112 Authorities that responded, the following figures are interesting:

Number of Board Members	Years Served
174	Over 10
65	Over 15
27	Over 20

The average period of years served by board members was 7.24 years. This is approximately 1-1/2 times the maximum term for which a board member may be appointed: five years. The average number of years of service represented on an Authority board by all board members was 38.22 years. Authority board members are constantly being reappointed by the incorporating municipality or municipalities. One Authority has four board members who have each served 26 years, and one member with 15 years. Another has three members each with 25 years' service and one member with 20 years and one newly appointed member. The Authority vehicle has made it possible for persons with community interests to serve their community when they would not actively seek election to any office. Of the members of Authority boards, 10% were members of professions, 15.9% were executives, 22.8% were self-employed, 5% were bankers, 11.5% were engineers and manufacturers. The remainder were retired persons and persons in miscellaneous occupations. Most of these persons donate their services as a community venture, receiving only the amount which the municipality creating the Authority votes to pay them. Out of Authority studies, only two were paid \$150 per month, the highest amount paid. There was one at \$100, one at \$75 per month and 45 received no compensation whatsoever. The remainder were between \$10 and \$15 a month. Forty percent of all of the board members donate their time. The average amount received per board member per month is \$3.66.

Authorities have performed an essential local function establishing all their projects on the American principle "pay as you go." They have assisted in getting Federal grants and have acted as a tool of their local government. The Authorities Association's position is that Authorities do not have to be used under their proposed constitutional language but the fact that

over 1700 have been incorporated would indicate that the tool of government is popular and is serving the communities' needs.

Comments are heard frequently that an Authority is an expensive method of operation. The following must be remembered:

A. It must be economically feasible or bonds cannot be issued.

B. It serves where private industry or municipal government will not or cannot serve.

There has to be a sufficient return on the investment in order to market the bonds.

It also makes possible joint operation and makes possible an equitable assessment of the cost of improvement in a municipality where only a portion of the municipality is to receive the benefit. Illustrative of this are sewer installations which service only part of a growing and developing municipality and it would be inequitable to tax the entire township for the benefit which only a portion of the township receives. Under the proposal of the Pennsylvania Municipal Authorities Association, it would be possible still for the municipality to set up an operation without the appointment of an Authority. However, the Authority system makes available the skilled judgment of persons in the community, usually without cost or with a minimum of cost to the municipality, and relieves the local government officials of a tremendous amount of detail work.

A study of the interest rates of Authorities vs. municipal operation is important. Over the past thirty years, Authority bonds have become recognized as a method of investment and the bonds of Authorities are rated according to the performance of that Authority. This has resulted in the difference in interest rates which at one time were stated to be greater than for comparable municipal issues and which difference is now non-existent.

The effect of this increased acceptance of Authority bonds may be seen in the following table. These figures compare the average yields on the 20-year bonds of local school authorities in Pennsylvania which have a rating of "A" by Moody's Investors Service, with the average figures for the "Bond Buyer's Index" for the same year.

	1960	1963	1965
<i>Average 20th</i>			
<i>Year Yield</i>	3.983%	3.300%	3.351%
<i>Bond Buyer's Index</i>	3.514%	3.166%	3.267%
<i>Difference</i>	.469%	.134%	.084%

It should be pointed out that some Authority bonds enjoy much lower interest than general obligation bonds and that the foregoing are averages rather than statements of individual issues.

The conclusion from this is that Authorities have now come of age and are accepted by investors. They are likewise accepted by local municipalities as a tool of government which is flexible, has adequate safeguards, gives an opportunity for community leaders to participate. With this background,

there can be only one conclusion in the opinion of the Pennsylvania Municipal Authorities Association and that is that the continued formation and operation of Authorities should be permitted on a permissive basis and that if a municipality feels that it can handle and operate a particular project on a basis more satisfactory to it, it should have the right to do so. All of this is possible under the proposals above set forth of the Pennsylvania Municipal Authorities Association.

Respectfully submitted,

s/ John T. Hoffman

President

s/ Charles A. Lucisano

First Vice President

s/ Herbert L. Walborn

Second Vice President

s/ Frank E. Heller

Immediate Past President

All of the above constituting the Executive Committee of the Pennsylvania Municipal Authorities Association.

*Proposals for Constitutional Revision by the Pennsylvania
Local Government Conference, Presented to the
Constitutional Convention Preparatory
Committee, July 27, 1967*

Probably no single group has as much to gain or lose in Constitutional Revision in Pennsylvania as do its local governments. Realizing this, the Pennsylvania Local Government Conference, the organization representing all the local governments of the Commonwealth—cities, boroughs, townships, counties and school districts—feel that it is necessary that the Committee and the Convention receive five basic principles for Constitutional Revision which all local governments agree are of paramount importance in revision. Individual associations will undoubtedly be supplementing these with proposals of their own, but we stress that these principles are ones which all local governments in Pennsylvania feel are necessary for a modern framework of local government in our Commonwealth.

RESIDUAL POWERS FOR LOCAL GOVERNMENT

Pennsylvania local governments traditionally have been the subject of the judicial principle referred to as "Dillon's Rule." It provides that local governments may exercise powers only specifically granted to them by the state constitution or by legislation. This has often resulted in local government being unable to adapt to change and puts a burden on the legislature and the courts. It is the position of the Conference that the trend toward turning to the state and federal governments by local government is often the result of not being able to meet adequately their responsibility because of the strict interpretation of local government powers brought about by Dillon's Rule and the lack of residual powers.

The Advisory Commission on Intergovernmental Relations supports this principle and it is its wording which is generally followed in the specific recommendation below:

"Cities, boroughs, townships and towns shall have all residual functional powers of government not denied by this constitution or by law. Denials may be expressed or take the form of legislative pre-emption and may be in whole or in part. Express denials may be limitations of methods or procedure. Pre-empted powers may be exercised directly by the state or delegated by law to such subdivisions of the state or other units of local government as the legislature may by law determine."

NO CONSTITUTIONAL DEBT LIMITS

The Conference believes that Constitutions should be flexible documents and that restrictions which can be easily outdated by changing conditions, such as debt restrictions, are better set by the legislature. Actually, the most effective limits on debt are the realities of the bond market. The Conference recommends that the subject of debt limitations should contain only a general grant of power to the legislature to regulate local government debt.

The Advisory Commission on Intergovernmental Relations suggests the following provision on the subject, which the Conference approves:

"The legislature may pass laws regulating the taxing and borrowing powers of political subdivisions of the Commonwealth."

REMOVAL OF EXEMPTIONS

One of the great contributors to the "squeeze" on local governments is the present system of property tax exemptions in our Commonwealth. As demands for service and costs increase, local governments are often faced with a decreasing property tax base because of continual extensions of property tax exemptions. This fact has forced local governments to turn to other, less equitable taxes, and to the state and federal government for help. It is not unusual for one-third of the property in Pennsylvania municipalities to be tax exempt.

The Conference feels that all property owners should pay their *fair share* for local services, and therefore propose the elimination of all exemptions on property, including governmental and authority exemptions. The Conference supports this in order to eliminate loop-holes through which those interested in not bearing their fair share can obtain exemptions. The Conference feels that only through this complete prohibition can the costs of providing services to property owners through property taxation be equitably distributed.

The Conference realizes that the uniformity clause of Section 1, Article IX, cannot be considered at the Convention, but wonders if an addition to that clause may not be feasible. It suggests the following wording be added to Section 1, Article IX:

"All taxes shall be uniform upon the same class of subjects, within the territorial limit of the authority levying the tax, and shall be levied and collected under general laws; such general laws shall provide for no tax exemptions on property, including all property owned or leased by the Commonwealth, its agencies, and its political subdivisions."

LAWS ON WAGES, HOURS AND WORKING CONDITIONS OF LOCAL EMPLOYEES

In every session of the Pennsylvania General Assembly there are hundreds of bills introduced and dozens of bills passed pertaining to wages,

hours and other working conditions of local government employees. The Local Government Conference feels that this type of legislation is detrimental to the orderly conduct of local government by the people elected to do this job—councilmen, supervisors, commissioners. These are the men who know local conditions, who are responsible for raising the revenue to provide for salaries, who must allocate limited resources to the best possible use for all. If the power to regulate the personnel policies of their own employees is taken away from the elected local official, what remains?

The Conference also feels that such legislation is detrimental to the General Assembly. A disproportionate amount of time and energy is spent by the body on these local problems; special interest group pressures in this area of legislation are often extreme and wearing on the individual legislator; time and effort of local officials are wasted in efforts to combat passage of this type of bill.

Often this type of legislation does not serve the best interests of those proposing it. Extreme pension demands when overstrained pension funds are involved is an example of this.

In summary, the Conference believes that the best interests of all concerned would be served if local governments were given the exclusive right of passage of laws concerning the wages, hours and working conditions of its own employees.

"Local Governments shall have the exclusive power to provide for the wages, hours and conditions of employment of local employees."

OPTIONAL CHARTERS FOR CITIES AND BOROUGHES

The Conference feels that it is important to provide limited home rule government for urban municipalities. Cities and boroughs differ greatly in Pennsylvania; they differ in size, population, economic base, wealth, etc. It is difficult to impose successfully one or two forms of government on all.

In the last half of the twentieth century, and for years after, the Conference feels that flexibility in local government structure may be the most important element in a municipality's ability to cope with change and the increased role it will be called on to play in serving its citizenry. It is the position of the Conference that limited home rule charter power through the use of optional forms of government provided by the legislature can be applied to all municipalities.

The Conference proposal generally follows the proposal of the Woodside Commission with the exception that it mandates legislative action by use of the word "shall"; under the optional "may" in the current constitutional provision on the subject, it took the legislature more than 25 years to provide optional charters for cities.

"The General Assembly shall, by general law, provide optional plans of municipal organizations and government for cities and boroughs under which an authorized optional plan may be adopted or abandoned by majority vote of the qualified voters of the city or borough voting thereon."