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Bankruptcy not a panacea for Luzerne County's ills

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Bankruptcy is often tossed out as a potential fix for Luzerne County government's chronic financial woes — a chance to "give us a clean slate" — as one taxpayer described the option at a county meeting several years ago.

Online commenters routinely portray bankruptcy as a panacea that would get the county out of paying some of its $368 million in outstanding debt and throw out union contract requirements and pensions guaranteed by law.

But Gerald Cross, executive director of the Pennsylvania Economy League that served as a consultant to several distressed municipalities, said there's no guarantee any of these drastic alterations would happen.

Instead, a bankruptcy could result in court-ordered property tax hikes far exceeding increases that would be passed by elected county council members, Cross said.

In Jefferson County, Alabama, for example, a 2011 bankruptcy resulted in sewer creditors agreeing to reduce $1.4 billion owed to them, and the county refinanced the remaining $1.8 billion. However, a bankruptcy judge approved a plan to significantly raise sewer rates annually to pay off the new debt over 40 years. Many residents protested the hikes, with some filing a still-pending legal challenge.

"It's important to solve the problem locally because you don't know what you will get if decisions are taken out of the hands of the county administration and elected officials," Cross said.

Many also have the mistaken impression a county bankruptcy would resemble personal bankruptcies that wipe out debt or corporate bankruptcies where assets are liquidated to pay creditors, Cross said.

Municipalities are treated differently because they can't shut down or sell most property and must continue providing mandated services, Cross said.

In Luzerne County that would include handling 911 calls, housing inmates, adjudicating criminal and civil court matters, running elections, maintaining a property tax base and hundreds of roads and bridges and shouldering some of the cost of services for the elderly, addicted and abused.

"A bankruptcy won't get the county out of mandates because government has a responsibility to continue operations," Cross said.

Bankruptcy rules also differ by state, and Cross said Pennsylvania municipalities must obtain state approval.

Harrisburg's 2011 bankruptcy filing was thrown out after state legislators barred it. A state-appointed receiver guided the city through a recovery plan that included the sale of parking revenue bonds and leasing of public parking spaces.

Cross said he doesn't believe a bankruptcy would be approved unless a county went through the Act 47 recovery program for distressed municipalities and was still unable to cover obligations after expenses and income were scrutinized and modified.

Others struggling

Doug Hill, longtime executive director of the County Commissioners Association of Pennsylvania, said most of the state's 67 counties are "having a difficult budget year."

"I don't think anyone is talking about bankruptcy," Hill said.

Several counties — including Luzerne — are participating in the state's early intervention program, which provides funding to help obtain outside analysis on options to improve finances. The program is aimed at preventing counties from entering into full-blown Act 47 distressed status, he said.

Public Financial Management, or PFM, the nation's largest independent financial adviser to state and local governments, completed long-term financial recovery plans for the county in 2004 and 2009 and is working on an update that will pinpoint new options available due to the county's 2012 switch to a customized home rule government.

Hill said many counties are struggling with sluggish revenue tied to the economy, more than a decade of stagnant state funding, issues with 911 funding formulas that put more burden on county taxpayers and their inability to use sales taxes or other alternative taxes to reduce reliance on property taxes.

Most county pension plans are in "relatively good shape" because the benefits, which are governed by state law, are not "extravagant" and officials have been "fairly diligent" overseeing investments and maintaining taxpayer subsidies, he said.

Next year's Luzerne County pension fund subsidy is estimated to increase from $8.4 million to $10.2 million, and years of continued taxpayer contributions are anticipated to close a gap between assets and liabilities, officials say. However, the county employee retirement system is more than 80 percent funded, compared to 59 percent in the state pension system, officials say.

Making progress

County Manager Robert Lawton said he does not believe the county is anywhere near a dire situation warranting bankruptcy.

The county's debt repayments are a "big stone in our throat," increasing $1 million to $28.6 million next year — an expense that eats up 22 percent of the proposed $129.26 million 2015 budget.

But the county has reduced health insurance costs and weaned off one-time fixes, such as using borrowed funds to cover operating expenses and obtaining cash advances on back-tax receipts, Lawton said.

The county also has not exhausted its option to generate revenue from taxes, he said.

County taxes went up 2 percent in 2012 and the home-rule maximum of 8 percent this year, but there was no hike in 2013 and a request of 4 percent for next year.

Another option

The county also could instantly avoid next year's 4-percent hike by getting rid of a discretionary tax break on primary residences that costs the county about $4.5 million annually.

Former county controller Walter Mitchell had suggested this option, but a majority of council members have not rallied behind cutting a popular break that saves homeowners $57 on county taxes.

"People don't want to pay the bill, but we're not at the wall," Lawton said, predicting a county bankruptcy filing would be thrown out.

A bankruptcy also could negatively impact the county's ability to borrow or refinance down the road and have a ripple effect on the municipal bond market statewide, jacking up interest rates on funds borrowed in other counties, Lawton said.

Council Chairman Rick Morelli believes the county would have to show it was unable to pay bills for mandated services after maxing out tax hikes for several years to have a valid bankruptcy claim.

“We cut over 200 positions in three years and are not irresponsible with borrowing like our predecessors. I’m not saying we’re in great shape, but we’re in better shape than we were and are on the right track,” Morelli said.

“We’re going to be OK. It will just take time.”

More bankruptcies predicted

Kirk B. Burkley, an attorney with Pittsburgh-based Bernstein-Burkley, P.C., which specializes in bankruptcies and restructuring, believes more cash-strapped local governments will consider bankruptcy if Detroit bounces back as he expects.

The city shed billions of dollars in debt and is now on “solid financial footing” for the first time in decades, he said.

“I think Detroit is going to be wildly successful, and more municipalities might see the benefits,” Burkley said.

Government entities that are constantly “kicking the can down the road” and operating in “crisis mode” can’t strategically plan for the future and “focus on the things that really matter,” he said.

Stressing he can’t comment on Luzerne County’s situation, Burkley said bankruptcies can allow municipalities to restructure union contracts and pension benefits and erase some debt. It’s not a “magic wand,” he cautioned.

“It will be an expensive, arduous process, and unions and pension holders and bond insurers will fight you on it, just like what happened in Detroit,” said Burkley, who disagrees that state approval is mandated in municipal bankruptcies in Pennsylvania.

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