

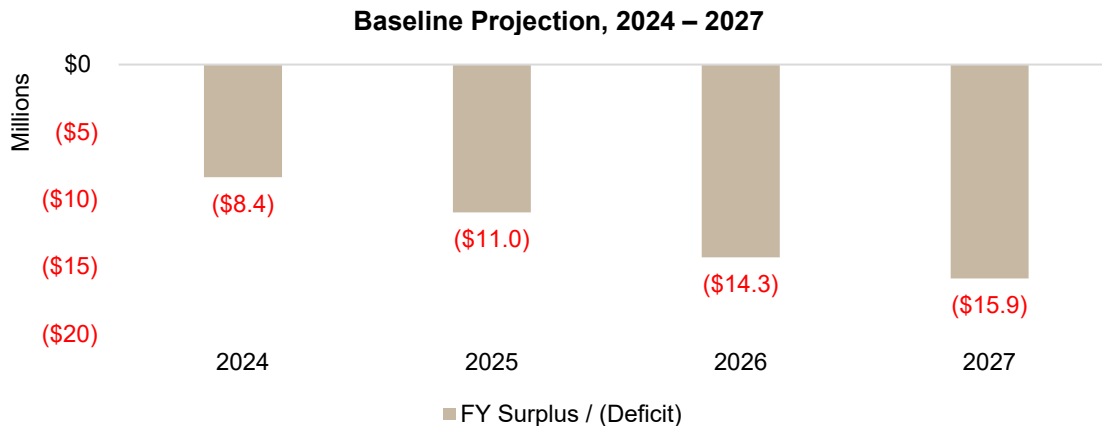


To: Mayor Barbarann Keffer
From: Gordon Mann, Lauren Sukovich, and Garrett Hincken; PFM
Re: **Updated Earned Income Tax Projection**
Date: November 22, 2023

Earlier this summer, we completed work on a multi-year financial plan for Upper Darby Township. This work followed your request to the Pennsylvania Department of Community and Economic Development for technical assistance as you recognized the Township’s growing financial challenges.

We evaluated the Township’s recent financial performance and found Upper Darby had deficits in its primary operating fund each year from 2018 through 2021¹. That string of deficits exhausted most of the Township’s reserves, leaving Upper Darby with just \$0.1 million in unassigned fund balance (i.e. the portion of a government’s reserves with the most flexible use) at the end of 2021. The Township finished 2021 with \$1.5 million in cash and cash equivalents, down 83.8 percent from 2018.

We also provided a baseline projection of financial results in a status quo scenario, assuming no changes in tax rates, headcount, or service offerings. That baseline projection showed a structural deficit where recurring expenditures grow faster than recurring revenues. If the Township does not take corrective action, then deficits will return in 2024 or 2025, depending on whether the Township uses its ARPA funding one more time to cover a potential deficit next year.



As we described in our analysis, these deficits are driven in part by Upper Darby Township’s reliance on one relatively flat revenue source – its real estate (or property) tax – to generate most of its operating revenue. Slow-growing property tax revenue is common for Pennsylvania municipalities; however, Upper Darby is more reliant on this source of revenue than other municipalities because the Township does not currently levy an EIT.

Pennsylvania law authorizes Upper Darby to tax the earnings of residents, regardless of where they work (resident EIT), and tax the earnings of non-residents who work in Upper Darby (non-resident or commuter EIT). Upper Darby is the only municipality of its size in Pennsylvania that does not use these taxes. Across the Commonwealth, Upper Darby is in a small minority as about 97 percent of Pennsylvania’s municipalities levied the EIT in 2023, along with hundreds of school districts.

¹ As of June 2023, the Township was working to finalizing its 2022 year-end external audit. All 2022 figures shown in this Plan are budgeted amounts unless otherwise noted.

Given the Township's deteriorating financial position, the magnitude of the projected deficits, and the practical difficulty of trying to balance a budget with growing expenditures on one side and flat revenue on the other, we recommend the City implement a resident and non-resident (i.e. commuter) earned income tax.

The Plan recommendation that explains the new EIT (Initiative RV01, pages 51-57) referenced an earlier projection of how much revenue that resident and commuter EIT would generate². That projection was completed in 2021 and used the most recent data available at the time, but that data was already a couple years old in 2021 and predated the COVID-19 pandemic.

At your request, we have updated that analysis so Upper Darby has a more recent projection for potential revenue generated by a new EIT. We've also provided additional detail on how many Upper Darby residents would experience a tax increase versus a tax shift (i.e. paying the same amount in taxes, but to different governments).

Our updated projection and analysis follows. If you have any questions, ideas, or concerns after you've reviewed our analysis, please contact Gordon Mann at 215-557-1439 or mann@pfm.com.

Methodology

To estimate the revenue that an EIT would generate, PFM conducted analysis drawing on several data sources:

- US Census Bureau, Longitudinal Employer-Household Dynamics (LEHD) 2021
- US Census Bureau, American Community Survey, Public Use Microsample (PUMS) 2017-2021
- US Bureau of Labor Statistics, Consumer Price Index for All Urban Consumers (CPI-U) 2023
- US Bureau of Labor Statistics, Current Employment Statistics (CES) 2023
- US Bureau of Labor Statistics, Local Area Unemployment Statistics (LAUS) 2023
- Pennsylvania Department of Community and Economic Development tax rates (DCED) 2023

These were the most recent Census Bureau and BLS data sets available as of November 14, 2023.

PFM used the LEHD data to identify the home and work census blocks of all workers who either lived or worked in Upper Darby in 2021. Since the LEHD data only classifies workers into three broad income categories, we calculated earnings using 2021 PUMS data for the home area of each worker. Estimates were adjusted to 2023 values using CPI and employment data from the BLS. We then calculated the estimated EIT revenues by applying either a 0.5% or 1% rate as would apply based on the home and work jurisdictions of the worker.

The analysis presented here is our best estimate of likely revenue that would be generated on an annual basis by a resident and commuter EIT. Our projections are also broadly consistent with the separate analysis conducted by Keystone Collections group using different data sources.

Results

Based on estimated 2023 employment and earnings, an Earned Income Tax in Upper Darby would return approximately \$9.0 million in revenue at a rate of 0.5% and approximately \$17.9 million at a 1.0% rate (Table 1).

In either scenario, slightly more than three-quarters of the total revenue would come from Upper Darby's residents, with the remainder generated by commuters who work in the Township. A little more than a third of revenue would come from residents who are already paying the tax at their place of work. Most of those residents would see no change in their tax liability, but the revenue would go to Upper Darby instead of the municipality in which they work.

² Econsult Solutions Incorporated (ESI) provided the EIT projection during their 2020 – 2021 engagement.

Table 1: Summary of Total Estimated EIT Revenue to Upper Darby

Type of EIT Revenue	Taxable Workers	0.5% EIT Revenue	1% EIT Revenue	Share of Workers	Share of 0.5% EIT Revenue	Share of 1.0% EIT Revenue
Upper Darby Residents	22,436	\$6,839,000	\$13,678,000	79%	76%	77%
Not paying any EIT now	12,683	\$3,701,000	\$7,403,000	45%	41%	41%
Paying EIT elsewhere (excl Phila)	9,753	\$3,138,000	\$6,275,000	34%	35%	35%
Upper Darby Non-Resident Workers	5,834	\$2,134,000	\$4,176,000	21%	24%	23%
Total Revenue to Upper Darby	28,270	\$8,973,000	\$17,854,000	100%	100%	100%

Table 2 shows a more detailed breakdown of taxpayers based on their home and work locations. Under EIT rules, a taxpayer's home municipality has priority over their workplace municipality *except* where either of those locales is the City of Philadelphia, which has the ultimate priority under the Sterling Act.

For the Upper Darby's residential EIT, that means the earnings of all workers living the Township would be taxable unless they work in Philadelphia.³ For those residents already paying EIT to their workplace, nearly nine of out 10 would see no change in their tax bill. For Upper Darby's non-residential EIT, that means a commuter would only pay EIT to Upper Darby if their home municipality either does not levy a residential EIT or levies an EIT rate of less than one percent, in which case the remainder up to 1% would be subject to Upper Darby's non-resident EIT. For out-of-state commuters to Upper Darby, the tax is levied at the full rate.

Table 2: Total Estimated EIT Revenue to Upper Darby

Home	Workplace	Current	EIT Tax under 0.5% and 1% Scenarios	Taxable Workers	0.5% EIT Revenue	1% EIT Revenue
Upper Darby	Upper Darby	Do not currently pay any EIT	Would pay 0.5% or 1% of earnings to Upper Darby	2,756	\$688,000	\$1,376,000
Upper Darby	Other PA municipality that levies a 1% EIT	Currently pay % of their gross earnings to other municipalities	No change for taxpayer, but first 0.5% or all 1% of revenue to Upper Darby	8,051	\$2,598,000	\$5,196,000
	Other PA municipality that levies an EIT <1%		Tax rate would increase to 1%, with first 0.5% or all 1% of revenue to Upper Darby	1,090	\$341,000	\$682,000
	Other PA municipality that levies an EIT >1%		No change for taxpayer, but first 0.5% or all 1% of revenue to Upper Darby	612	\$199,000	\$397,000
Upper Darby	Other PA municipality that has no EIT	Do not currently pay any EIT	Would pay 0.5% or 1% of their gross earnings to Upper Darby	9,927	\$3,013,000	\$6,027,000
Other PA municipality with no EIT or EIT <1%	Upper Darby	May pay resident EIT to their home municipality	Tax levied between home municipality rate and 1% remitted to Upper Darby - only a change for worker if the old tax rate was < 1%	4,568	\$1,718,000	\$3,344,000
Outside PA	Upper Darby	Do not currently pay any EIT	Would pay 0.5% or 1% of their gross earnings to Upper Darby	1,266	\$416,000	\$832,000

³ PFM also excluded residents commuting to other states from our analysis, as any income taxes paid to those jurisdictions could be credited against their EIT liability. Estimates of the number of non-taxable residents and workers are presented in Table 3.

Total	28,270	\$8,973,000	\$17,854,000
<i>Residential</i>	22,436	\$6,839,000	\$13,678,000
<i>Non-Residential</i>	5,834	\$2,134,000	\$4,176,000

Table 3 shows the composition of the workers living or working in Upper Darby that would not be subject to the township's EIT because of their residence or workplace location. That includes workers commuting to and from the City of Philadelphia, and commuters to Upper Darby from municipalities with an EIT of 1% or greater. Upper Darby residents commuting to jobs out of state were also excluded under the assumption that any resident EIT they might pay would be offset by credits for income taxes paid to other states.

Table 3: Total Non-Taxable Workers Living or Working in Upper Darby

Home	Workplace	Current	EIT Tax under 0.5% and 1% Scenarios	Non-Taxable Workers
Upper Darby	Philadelphia	Current pays Philadelphia non-resident wage tax	Will continue paying Philadelphia non-resident wage tax	11,257
Upper Darby	Outside PA	May pay income taxes to other states	Assumed offset by credits for out-of-state income taxes paid	2,969
Philadelphia	Upper Darby	Currently pays Philadelphia resident wage tax	Will continue paying Philadelphia resident wage tax	4,745
Other PA municipality with EIT >=1%	Upper Darby	Currently pays to their home municipality	Will continue paying resident EIT to their home municipality	4,607
Total				23,578

Note that the population of in-commuters paying to their home municipality could grow (and conversely, the number of taxable non-residents would shrink) if other municipalities in the area were to introduce resident EITs of their own.

Table 4 shows the top 20 municipalities in terms of estimated non-residential EIT revenue that would be paid to Upper Darby. Commuters from these municipalities comprise approximately 90 percent of the non-resident EIT that comes from Pennsylvania residents.

Table 4: Top 20 Other PA Municipalities by Estimated Non-Resident EIT to Upper Darby

Rank	Home County	Home Municipality	Workplace	Number of Workers	0.5% EIT Revenue	1% EIT Revenue
1	Delaware	Haverford Township	Upper Darby	746	\$345,500	\$691,000
2	Delaware	Marple Township	Upper Darby	407	\$193,700	\$387,400
3	Delaware	Springfield Township	Upper Darby	457	\$149,300	\$298,500
4	Delaware	Ridley Township	Upper Darby	448	\$126,600	\$253,100
5	Montgomery	Lower Merion Township	Upper Darby	209	\$103,600	\$207,300
6	Delaware	Newtown Township	Upper Darby	153	\$79,700	\$159,400
7	Delaware	Upper Providence Township	Upper Darby	114	\$61,900	\$123,800
8	Delaware	Middletown Township	Upper Darby	129	\$61,100	\$122,300
9	Montgomery	Upper Merion Township	Upper Darby	105	\$50,800	\$101,500
10	Delaware	Clifton Heights Borough	Upper Darby	171	\$43,400	\$86,700
11	Delaware	Nether Providence Township	Upper Darby	111	\$42,300	\$84,500

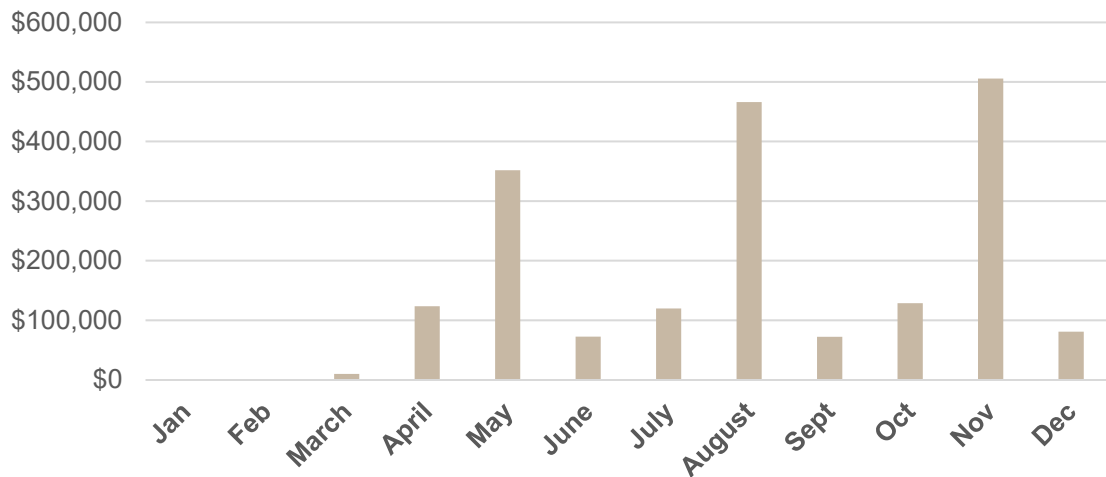
Rank	Home County	Home Municipality	Workplace	Number of Workers	0.5% EIT Revenue	1% EIT Revenue
12	Delaware	Lansdowne Borough	Upper Darby	186	\$40,100	\$40,100
13	Delaware	Radnor Township	Upper Darby	82	\$36,800	\$73,600
14	Delaware	Darby Township	Upper Darby	148	\$35,200	\$70,300
15	Delaware	Concord Township	Upper Darby	66	\$33,600	\$67,200
16	Chester	Tredyffrin Township	Upper Darby	69	\$30,100	\$60,300
17	Delaware	Collingdale Borough	Upper Darby	126	\$29,700	\$59,400
18	Delaware	Bethel Township	Upper Darby	51	\$22,900	\$45,900
19	Delaware	Aldan Borough	Upper Darby	89	\$22,700	\$45,400
20	Delaware	Norwood Borough	Upper Darby	86	\$21,900	\$43,900

Additional considerations

Our analysis shows the projected annual revenue from a new resident and commuter EIT at either 0.5 percent or 1.0 percent. We note three factors that could reduce Upper Darby's projected revenues, one of which would only apply in the first that the tax is levied.

- Time lag:** Some communities have received less revenue on a cash basis than projected in the first year of their new or increased EIT rate. This is due to the time lag between the point at which the new tax takes effect and the point at which the Township receives revenue from that associated tax. For example, the graph below shows the City of Chester's earned income tax revenue from the new distressed pension EIT that took effect on January 1, 2021.

**City of Chester Distressed Pension EIT
First Year of Implementation**



Chester's distressed pension EIT on residents now generates \$800,000 to \$900,000, but it took a couple quarters to reach that level of revenue generation. There was very little revenue during the first quarter that the tax was in place. Revenues were better, but still not at their full level in the second quarter, presumably because employers were still adjusting withholdings to the correct rate.

Please note that this time lag could result in revenue delayed, but not revenue lost. Taxpayers were required to make up for any missed tax payments during 2021 when they filed their tax returns in 2022. This timing-related discount only applies in the first year that the tax takes effect.

- Neighboring Municipality EIT:** While Upper Darby is in a shrinking minority of Pennsylvania municipalities that do not levy an EIT, several of its neighbors in Delaware County also do not have the tax. More than a quarter of the 87 municipalities (out of more than 2,500) that do not use the

EIT are in Delaware County. If the Township enacted an EIT, commuters to Upper Darby who live in these townships would pay the commuter (or non-resident) tax to Upper Darby. If those neighboring Townships started implementing their own resident EIT, Upper Darby's non-resident revenue would drop as taxes are first remitted to a commuter's home municipality.

- **School District Taxing Powers:** Pennsylvania law allows school districts to 'split' the first 1.0 percent of a resident earned income tax with municipalities. Upper Darby School District does not currently levy an EIT, but it could decide to levy one and split this with the Township in the future. Non-residents would still pay the tax to the Township since school districts cannot tax commuters.

Township leaders should meet with the Upper Darby School District to see if it intends to split the resident EIT.⁴ The split does not happen automatically. The School Board would have to take separate action to claim its share. It is important to know if the School District will take its portion of the resident EIT since that will impact how much revenue the Township receives.

⁴ We do not recommend that the Township enact a resident EIT rate higher than 1.0 percent at this time but, if that did happen, the School District would only split the first 1.0 percent of the resident EIT. For example, if the Township had a 1.2 percent resident EIT rate, the School District would get 0.5 percent (half of the first 1.0 percent) and the Township the remaining 0.7 percent.