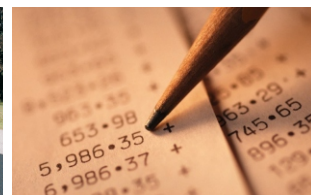


# Municipal Authorities in Pennsylvania

> ready > set > succeed



# Municipal Authorities in Pennsylvania

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Ninth Edition  
August 2002

Comments or inquiries on the subject matter of this publication should be addressed to:

Governor's Center for Local Government Services  
Department of Community and Economic Development  
Commonwealth Keystone Building  
400 North Street, 4<sup>th</sup> Floor  
Harrisburg, Pennsylvania 17120-0225  
(717) 787-8158  
1-888-223-6837  
E-mail: ra-dcedclgs@state.pa.us

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Douglas E. Bilheimer, Executive Director, Pennsylvania Municipal Authorities Association

John W. Brosius, Deputy Director, Pennsylvania Municipal Authorities Association

Robert W. Naef, Executive Manager and Chief Engineer, Chester Water Authority

George M. Aman, III, Legal Counsel, Pennsylvania Municipal Authorities Association

William A. Atlee, Jr., Controller/Asst. Executive Manager, Chester Water Authority



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# I. What and Why of Authorities

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## Emergence of Authorities

Authorities (also known as special districts in other states) are governmental bodies created to finance and/or operate specific public works projects without tapping the general taxing powers of the municipality. Initially this was done through a device known as the revenue bond where revenues generated from users of the project pledged to operate it, maintain it and make the payments of principal and interest on the debt incurred to build it. The first modern attempt at revenue bond financing in this country appeared in Spokane, Washington in 1895. There was a second attempt in Chicago in 1898. During the period from 1910 to 1925, municipal revenue bonds became an established method of financing in the United States. By 1932, water revenue bonds had been issued by municipalities in about 10 states.

The revenue bond mechanism was next extended to special-purpose public entities. The Port of London, organized in 1909, was the first authority to be known by this name. The name authority was said to have been given by a newspaper editor as a reaction against the many 'authorities' granted to it by Parliament. The Port of New Orleans, organized in 1896, was the first modern-type authority in the United States, although it did not carry the name authority in its corporate title. The Port of New York Authority has the distinction of being the first American institution to use this term. Formed jointly by the states of New Jersey and New York, it resolved long-standing disputes over the control of maritime traffic in the Hudson River and New York Harbor. Organized in 1921, its financial success, following a shaky start, has done much to encourage authority creation in other areas.

Municipal authorities in Pennsylvania, as in many other states, had their beginning in the Depression of the 1930's. As part of its fiscal recovery policy, the federal government granted money to states and municipalities for public works construction to stimulate employment and provide needed public facilities. These grants had to be matched by the recipient unit, but many states and localities were unable to pay their shares, due both to reduced revenues and restrictive debt limits. A number of states, including Pennsylvania, then created state authorities to borrow outside constitutional debt limits by making use of revenue bonds. Pennsylvania was one of three states that passed general enabling legislation to allow their municipalities to create authorities. This was the Municipalities Authorities Act of 1935.

The 1935 Act was repealed and replaced in 1945 by the present Municipality Authorities Act giving greater flexibility in operation and in the type of bonds issued. The text of the Act is printed at the end of this book. It retains the same principles. The project must be in the proprietary fields of government, must have a public interest and must be self-sustaining. The requirements of public interest and self-sustaining nature are basic in understanding authority operations.

Approximately 200 municipal authorities were organized under these acts prior to 1951. In 1951, the way was cleared for leaseback authorities by a decision of the Pennsylvania Supreme Court upholding the right of municipalities to sign long-term leases with authorities.<sup>1</sup> This additional flexibility allowed authorities to borrow on the pledge of rentals made by the municipality over the term of the bond issue. The municipality would operate the project with its own employees and use the revenues collected to make the lease rental payments to the authority.

The number of authorities formed annually peaked in the 1950's, but activity in the amount of bonds issued annually did not reach a peak until 1986. In the 1940's borrowings were heaviest for water authorities, in the 1950's and 1960's for school authorities and since 1975 for hospital authorities. Issuance of sewer debt has been important since 1950, but it was the largest category only in 1974 and 1986.



## Character of the Authority

The municipal authority in Pennsylvania is an alternate vehicle for accomplishing public purposes rather than through direct action of counties, municipalities and school districts. The Municipality Authorities Act of 1945 describes an authority as “a body corporate and politic” authorized to acquire, construct, finance, improve, maintain and operate projects, provide financing for insurance reserves, make loans, and to borrow money and issue bonds to finance them.<sup>2</sup>

Although local government plays a role in creation of an authority and appoints the members of its board, the authority is not part of the municipal government. An authority is not the creature, agent or representative of the municipality, but is an independent agency of the Commonwealth.<sup>3</sup> It is a public corporation engaged in the administration of civil government. An authority is a separate legal entity with power to incur debt, own property and finance its activities by means of user charges or lease rentals. An authority can be a financing agent for a capital project, an operating entity or both. Authorities finance a significant share of local capital improvements.

## Reasons for Creating Authorities

**Financial Reasons.** Pennsylvania local governments were faced with unrealistic debt limits based on real estate values before the implementation of reforms mandated by constitutional amendment in 1972. The Local Government Unit Debt Act now sets limits based on average total revenues of the local government. Self-liquidating debt funded entirely from project revenues can be excluded from the municipality's debt limit. This change, plus the inclusion of outstanding lease rental obligations owed to authorities in the overall determination of debt limits has removed any advantage accruing to the authority method of borrowing because of debt limit considerations. However, the previous debt limitations gave rise to many authorities now in existence.

Another financial consideration is the desire to avoid local tax increases. Authorities do this by resorting to user charges. User charges can result in a more equitable distribution of the burden of government by shifting costs to actual consumers with payments based on the level of service consumed. Municipalities can and do impose user charges, but authorities must employ this method since it is their only revenue source. It is easier for an authority to impose user charges because of its relative freedom from political pressure. Also, people may accept authority user charges more readily than those imposed by local governments in some areas where there is a lingering popular expectation government services should be free, that is, tax supported. An authority can be a device to achieve user cost financing when it is politically difficult for a local government to do so.

As governmental entities, authorities enjoy certain advantages over private companies operating services such as public water supply and solid waste disposal. As governments, they do not pay corporate taxes or sales taxes when they purchase supplies, they can issue tax-exempt debt at a lower rate than private corporations and their rate structure does not need to include a return to shareholders.

**Administrative Reasons.** Reasons grouped under this heading are based on the proposition an authority can administer certain entrepreneurial-type services more efficiently than a municipal government. Many functions commonly provided by authorities are in traditional areas of public utilities where business traditions and concepts of administration are needed. Authority functions often require intensive planning and a long-range approach more likely to be found in a business-type operation than in government.

Delegation of overseeing a complex function to a group of citizens other than the elected officials spreads the workload and responsibility for providing public services to a wider base in the community. It relieves some of the burden from the elected governing body, already responsible for overseeing a wide range of governmental functions. Since most authorities perform only one function, the authority board can concentrate its energies on this single area.

Removal of authority affairs from close popular control allows it to make decisions beneficial to the public in the long run, but possibly unpopular in the short run. Under the terms of their bond indentures, authorities must create reserves to provide sufficient funds to meet any emergency. Creation of prudent reserves is more difficult for elected officials who must offset the desire to maintain voter approval by minimizing costs against the demands of financial prudence.

Authority board members have five-year overlapping terms, thus ensuring a large measure of independence. Greater continuity of management personnel is also possible where the governing board does not have to face the electorate. An authority is able to select its own employees. Capable people can be attracted because tenure is more certain. There is no immediate change in office with elections.

Authorities can often attract more qualified people as board members. Often well-qualified individuals who would hesitate to run for elective office will agree to accept an appointment to serve on an authority board.

**Jurisdictional Reasons.** Many public services can be administered efficiently only if a large service area is covered. Political boundaries and the boundaries of this ideal service area seldom coincide. A joint authority, as a separate entity created by a number of municipalities, can provide a specific service for the larger area. It is not the only way to solve this problem, but it is politically acceptable, convenient and familiar to local officials and citizens. Water and sewer authorities commonly serve more than one municipality to take advantages of the economies of scale and natural drainage areas. Joint authorities are also used for such services as airports, recreation and mass transit.

## Distinctions between Authorities and Municipalities

Authorities have certain characteristics causing them to resemble a private utility corporation, but they also possess many features of a municipal government. It has become customary to speak of an authority as a government business venture. This is a reasonably accurate statement, if leasebacks are excluded. Municipal authorities resemble municipal governments in some ways.

1. They are exempt from taxation. This exemption applies to property owned and transactions conducted by the authority. Furthermore, interest on authority bonds is excluded from state and federal income taxes.
2. Authorities may levy and enforce special assessments against properties served.
3. Authorities possess the power of eminent domain to acquire real estate.
4. Municipal authorities may participate in the Pennsylvania Municipal Retirement System.
5. Authorities and municipalities are both subject to general state laws protecting the public interest, including the Sunshine Law, the Open Records Act and the State Ethics Act.

A municipal authority differs from a municipal government in a number of significant ways such as:

1. A municipal government is a “general purpose” unit of government, exercising powers of both a governmental and entrepreneurial nature. It has residual police powers to protect the public safety, health and general welfare. By contrast an authority exercises a limited entrepreneurial power only.
2. A municipal governing body is elected and subject to the express wishes of the voters. An authority board is appointed and thus some distance removed from the voters. An authority can raise and spend money without reference to the immediate wishes of the electorate, while government officials raising and spending money must face the voters at the next election.

3. A municipality has the power to tax and raise additional revenues through a wide variety of franchise fees, rents, user fees and service charges. Authorities are limited to the revenues generated by their project such as user charges, connection fees and special assessments.
4. Operating under the Municipality Authorities Act, authorities are free of many of the restraints that state law imposes on the administrative, budgetary and personnel practices of municipalities under the various municipal codes. While the Act does impose some restraints on the operations of an authority they are not as pervasive as those included in the municipal codes.
5. Most municipal authorities concentrate on a single service while municipalities offer a multitude of services. As limited by its articles of incorporation, an authority is restricted as to the functions it may perform and is relatively free as to the methods it may use in providing those services or functions. On the other hand, municipalities have multiple responsibilities. Municipal officials are relatively free in determining the services to be rendered but they are more restricted as to the methods employed in carrying out their activities.

## References

1. *Griffith v. McCandless Township*, 77 A.2d 430, 366 Pa. 309, 1951.
2. 53 PA.C.S. 5607; Municipality Authorities Act.
3. *Commonwealth v. Erie Metropolitan Transit Authority*, 281 A.2d 882, 444 Pa. 345, at 348, 1971; *Simon Appeal*, 184 A.2d 695, 408 Pa. 464, at 467, 1962; *Rhoads v. Lancaster Parking Authority*, 520 A.2d 122, at 126, 103 Pa.Cmwlth. 303, 1987; *Bristol Township Water Authority v. Lower Bucks County Joint Municipal Authority*, 567 A.2d 1110, at 1113, 130 Pa.Cmwlth. 240, 1989; *White Rock Sewage Corporation v. Pennsylvania Public Utility Commission*, 578 A.2d 984, at 987, 133 Pa.Cmwlth. 608, 1990.

## II. Creating and Dissolving Authorities

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An authority can be organized by any county, city, borough, incorporated town, township or school district of the Commonwealth, acting singly or jointly with one or more other local governments. Home rule municipalities must use the procedures found in the Municipality Authorities Act for creating, dissolving and withdrawing from authorities.<sup>1</sup>

Authorities may only be created for the purposes listed in the Act. However, the list contains a great variety of projects an authority may finance, own, operate or lease. These include water distribution systems, sewage systems, mass transit operations, parking facilities, airports, solid waste disposal systems, recreation facilities and school buildings. Projects to supply retail electric power, gas, telephone and cable television service are not included in the list although authorities may cogenerate electricity at their projects. The Act prohibits creation a new authority or expansion of an existing authority into a field that duplicates or competes with existing private enterprises serving substantially the same purposes.

### Creation of an Authority

**Determining Need.** A significant amount of planning and debate must be undertaken before a decision is made to incorporate a municipal authority. Normally the need to provide a service or significantly expand an existing service, be it water distribution and treatment, wastewater collection and treatment, solid waste collection and disposal or public transportation, is the driving force behind the debate. The local elected officials need to assess the alternatives for providing the service, the local government itself, a municipal authority or a private corporation. The decision will be impacted by the demands of federal and state statutes pertaining to and controlling the provision of many public services, including aviation, mass transit, sewer, water and solid waste. Another key element is the desirability of providing the service at a multi-municipal level. A determination initially **must** be made that the service is needed or required. The requirement for service can come from a various number of sources not the least of which are the courts or other regulatory agencies such as the Environmental Protection Agency (EPA) (at the federal level) or the Department of Environmental Protection (DEP) (at the state level). The need to modernize or consolidate a number of small, independent public or private agencies, such as small water supply systems, may be the driving force. Elected officials, planning commission members, citizens of the municipality or municipalities, businesses and property owners to be affected need to be heard during the planning process. The elected local government officials will make the final decision on how the service will be provided.

**Process.** When the governing body of a local government decides to create an authority, it adopts a resolution or ordinance expressing its intention. If it is to be a joint authority, each participating unit takes this action. The organizing local unit or units may specify the project or projects to be undertaken by the authority in the ordinance or resolution expressing its intention to incorporate an authority. No other projects can be undertaken by the authority. This can also be done from time to time by subsequent ordinance or resolution. If the local governing body does not specify a project or projects, the authority has the power to undertake any project authorized by the Act.<sup>2</sup> However, authorities created by school districts are restricted to construction of public school buildings and other projects for public school purposes. The resolution or ordinance of the elected governing body is then published in the local newspaper and legal periodical, along with a notice of the day the articles of incorporation of the proposed authority will be filed with the Secretary of the Commonwealth of Pennsylvania.

The articles of incorporation filed with the Secretary include the following items.

1. the name of the authority;
2. the name of the incorporating local unit or units;
3. the names, addresses and terms of office of the first members of the board of the proposed authority;
4. a listing of the authorities already organized by the incorporating local government, if any;
5. in the case of a business district authority, a statement that the municipal governing body retains the right to approve any authority plan for providing improvements or administrative services;
6. the authorized projects the authority may undertake;
7. the term of existence of the authority if it is other than the statutory maximum of 50 years, and
8. designation of the service area for the authority.

If the Secretary of the Commonwealth finds the articles of incorporation conform to law, a certificate of incorporation is issued and the existence of the authority begins from the date of the certificate and lasts for 50 years, but it may be extended by amendments to the articles of incorporation.

**The Authority Name.** The articles of incorporation must specify the name of the authority, a matter more significant than is generally realized. The name of the authority is its first point of contact with the public and the initial impression brought about by the name can be lasting. An overly long or complex name hinders communication. This is also significant when the authority borrows money for its project. It is helpful if the name chosen is readily recognizable as a known place name by people in the financial centers and the investing public who ultimately will be deciding on the terms and rates for lending money to the authority. It is also wise to avoid a name that could generate confusion in identity. In a state with 28 municipalities with Union as part of their name, 27 with Washington, 19 with Jackson, 15 with Pine and 13 with Jefferson, the potential for confusion is real.

## Merger of Authorities

The Municipality Authorities Act contains a procedure for the merger or consolidation of authorities, but this procedure is limited only to authorities whose projects are all leased to the same reorganized school district.<sup>3</sup> This provision was added in 1968 following the school consolidation process of the mid 1960s. It was intended to allow the new consolidated school districts to merge the authorities funding their building projects. The Act does not include a general provision governing merger of other types of authorities.

When it becomes desirable to merge other types of authorities, a more roundabout process must be followed. One way this can be done is for the municipality, or municipalities jointly, to create a new authority. In order to transfer the projects of the old authorities to the new one, the municipality or municipalities go through the procedure for assuming the project and then transfer it to the new authority. Then the old authority, with all its obligations paid off, can be terminated by the municipality or municipalities. This procedure sounds cumbersome but has been used a number of times. A second method is also available. Authorities have the power to convey any and all property they own to another entity. They are not limited to conveying their property solely to the incorporating municipality.<sup>4</sup> This can even be done when the authority still has outstanding debt. At times the bond indenture for authority debt will allow the project to be transferred to another authority which in turn assumes the indebtedness. Where this is not possible, the purchasing authority can issue new debt to defease the debt of the selling authority. For authorities with no outstanding debt, this is not a factor. The incorporating municipality has a contingent interest in the assets of the authority so the authority needs to

get its approval prior to the sale of the authority's project to a third party. The sale of an authority's project will not terminate the existence of the authority. That must be done following the procedure for termination outlined in the Act.

## **Joining or Leaving Joint Authority**

After a joint authority has been created, additional municipalities may become members of the authority. Occasionally a municipality, through its elected officials or staff, will express a desire to become a member of an existing authority; Section 3.1 of the Act details the procedures which must be followed.<sup>5</sup> The authority board members and elected officials of the joining municipality and the incorporating municipality(ies) must negotiate the terms for the entry of the additional municipality and reach a consensus. This is to include any reappointment of the authority board membership or revision of terms of office of its members. Unanimity among all concerned is required before the application is filed with the Secretary of the Commonwealth. The municipal governing body enacts an ordinance or resolution to join and the authority board and existing municipal members must formally consent to the joining. Notice must be published in a newspaper of general circulation and in the county legal journal. An application is filed with the Secretary of the Commonwealth with information similar to the original articles of incorporation. If the application conforms to law, the Secretary of the Commonwealth issues a certificate of joinder.

The same procedure must be followed for the withdrawal of a municipality from an existing authority. However, no municipality is permitted to withdraw from an authority after any financial obligation has been incurred by the authority.<sup>6</sup> These requirements do not apply where the municipalities only have operating agreements, but are not formal members of the authority.<sup>7</sup> When a municipality, for whatever reason, decides it wants to withdraw from a joint authority, it may do so by filing an application to withdraw with the Secretary of the Commonwealth. The authority board must formally consent to such withdrawal; procedures to withdraw are found in Section 3.1 of the Act. Essentially the formal procedures are similar to those used when incorporating an authority or when joining an authority. The Secretary of the Commonwealth, upon determining the application conforms to law, will issue a certificate of withdrawal.

The prohibition on withdrawing from a joint authority after any obligation has been incurred by the authority could raise other issues. The act does not define the term "obligation" as solely one pertaining to a financial commitment, such as bonded debt. If objections were raised to a request for withdrawal based on an obligation of the authority of type other than a financial obligation the matter would likely need to be resolved by the courts.

## **Assumption of Authority Projects by Municipality or Other Authority**

The local government or governments creating an authority may acquire any project of the authority by appropriate resolution or ordinance signifying this desire. On the assumption by the municipality of all outstanding obligations incurred with respect to the project, the authority will convey the project to the municipality. School projects may be acquired by the school district leasing them by the same method. Projects operated by a county authority for portions only of the county may be acquired by this method by the municipalities benefited with the approval of the county commissioners.<sup>8</sup> The courts have ruled municipalities can unilaterally act to take over an authority project, they do not need the approval of the authority board.<sup>9</sup> The municipality can even require the authority board to extinguish its outstanding financial obligations with existing authority funds.<sup>10</sup> Where there is outstanding debt that cannot be extinguished, the terms of the bond indenture can limit whether or not the debt is directly assumable by the municipality. The other choice is for the municipality to issue new debt to defease the outstanding authority debt. In assuming any outstanding debt, the municipality must follow the proper procedures under the Local Government Unit Debt Act.<sup>11</sup> The wording of this section

does not preclude the sale or transfer of its property to parties other than the incorporating municipality. The conveyance of a sewer project to an area-wide county sewer authority was upheld. In this case the trust indenture ensured the rights of the bondholders were protected.<sup>12</sup>

The local government assuming an authority project must have in place the administrative mechanism for managing the authority project, including trained personnel to operate it. The acquiring municipality receives the authority reserve funds that have been derived from the operation of the project. However, these reserves must be maintained in a separate fund and used solely for the purposes of operating, improving or extending the project. Any authority reserve funds representing the proceeds of borrowing must be maintained in a separate fund and used only for capital purposes. These provisions were added to the Municipality Authorities Act in 1996 to prevent municipalities from acquiring authority projects to get control of the reserve funds in order to use them for other municipal purposes.<sup>13</sup>

## **Privatization**

In recent years a growing national trend has been the transfer to the private sector of the operation of municipally owned water and sewer systems and other public facilities including prisons, solid waste management and others. In the past, privatization has been partial, limited to contracting of the management services for a publicly owned utility or outsourcing of certain functions of the utility's operation. Water and sewer utilities have historically contracted for certain operations such as installation of water mains, equipment rental and in some cases, meter readings, to name but a few. Some municipalities now feel that they can save money by contracting with a private firm to operate and manage the complete system and this has occurred with more frequency in the last ten years. The most extreme form of privatization is the outright sale of the public entity such as a water or sewer authority. In Pennsylvania, the need to upgrade water and sewer utilities to meet federal pollution control and drinking water standards has led to the sale of small, undercapitalized water and sewer authorities to privately owned utilities.

In Pennsylvania, authorities have a distinct financial advantage inasmuch as they are tax exempt and can issue tax-exempt bonds. To overcome this built-in advantage, the private sector, which must pay corporate taxes and dividends to its shareholders, can successfully privatize public services only where justified by the greater efficiency of their operations and the economies of scale achievable by their larger size. If the municipal utility or municipal authority being purchased is poorly managed and/or their revenues are insufficient to provide satisfactory service, then sale to a private utility or an adjacent authority that is larger and better managed can be beneficial.

In the case of the outright purchase of an authority system, the municipality that created the authority receives the net proceeds from the sale of the project after all debt has been paid. The amount of money being paid for authority systems is significant and can amount to tens of millions of dollars for medium size boroughs and townships. Unlike the assumption of an authority project by the municipality, the use of these funds is not restricted in any way. While this potential windfall is attractive, elected officials should remember the buyer will have to recover the investment of the purchase price and this could result in higher rates over the long term.

## **Termination of an Authority**

An authority may be terminated after the bonds and interest secured by the pledge of revenues from its project have been paid. The termination is subject to any agreements concerning the disposition of the project or other property owned by the authority. The authority board submits a certificate requesting termination of the authority to the local government that created it. After the elected governing body approves the certificate, it is

filed with the Secretary of the Commonwealth.<sup>14</sup> Upon termination, all property and other assets as well as any potential liabilities of the terminated authority pass to the incorporating local government and the authority ceases to exist.

Unless extended by articles of amendment filed in the Department of State, the authority's term of existence automatically expires after 50 years without any further local action. In most cases, the articles of incorporation are amended to extend the term of the authority before the expiration date. This almost always occurs when new bonds are issued or bonds are refinanced so that the maturity date of the bonds does not exceed the term of existence of the authority. Even where there is no outstanding debt, active authorities can use the amendment process to extend their term of existence.

**Inactive Authorities.** As of August 2001 there were 660 inactive authorities in Pennsylvania. These are authorities with no financial activity. A very small number of these are advisory boards or newly formed authorities whose projects have yet to be initiated. The vast bulk of inactive authorities have long since ceased operations and closed out their accounts. For most, no appointments to the board have been made for years. But without a formal termination in the Department of State, the authority remains in legal existence until its 50-year term expires. In cases of inactive authorities, the Department of State will accept Termination Certificates endorsed solely by the municipal governing body where the certificate includes a finding by the governing body that the authority has no board and its obligations have been paid off.

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2. 53 PA.C.S. 5607c; Municipality Authorities Act, Section 4.A(c); *Upper Dublin Township Authority v. Pizek*, 218 A.2d 328, 420 Pa. 536, at 540, 1966; *Shannon v. Ashton*, 75 D.&C.2d 318, at 320, 1975, C.P. Northampton Co.
3. 53 PA.C.S. 5606; Municipality Authorities Act, Section 3.3.
4. *County of Allegheny v. Moon Township Municipal Authority*, 671 A.2d 662, 543 Pa. 326, 1996.
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### III. The Authority Board

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#### Appointment

Municipal authorities are governed by a board whose members are appointed by the incorporating local government. The board members have overlapping five-year terms. When an authority is first created some of the original appointments are for shorter periods, so future vacancies occur each year. Boards may not consist of less than five members, and boards of joint authorities must contain at least one representative from each participating municipality. Allocation of representation on the board of a joint authority is agreed upon at the time the authority is created and is specified in the articles of incorporation. If an additional municipality later joins a joint authority, the articles of joinder must specify the representation of the new member municipality and any changes in the board membership allocation among the existing members.

**Terms.** Terms of board members expire on the first Monday in January. After a vacancy has occurred because of the expiration of a member's term, the municipal governing body appoints a member for a term of five years from the date of the expiration of the prior term.<sup>1</sup> These appointment provisions were amended in 1978 to prevent 'lame duck' municipal governing bodies from making appointments to authority boards for terms about to expire before a newly elected governing body took office on the first Monday in January.<sup>2</sup> Board members may succeed themselves.

**Vacancies.** If a vacancy occurs on the board due to death, disqualification, resignation or removal of a member, the municipal authority making the original appointment appoints a successor to fill the unexpired term.

**Removal.** A board member may be removed by the court of common pleas for cause, after at least ten days notice and a full hearing by the court. The municipal governing body has the power to remove a member of a board for missed authority board meetings. However, members of boards of parking authorities organized under the Parking Authority Law may be removed at the will of the appointing power. Unless excused by the authority board, a member of a board who fails to attend three consecutive meetings of the board may be removed by the appointing municipality up to 60 days after the date of the third meeting of the board which the member failed to attend.

**Qualifications.** An individual appointed to an authority board must be a taxpayer in, maintain a business in, or be a citizen of a municipality into which one or more of the projects of the authority extends or is to extend or to which one or more projects has been or is to be leased. Except for special service districts located in whole or in part in cities of the first class or on the board of a business improvement district of a borough, that was established on or before the effective date of this act, a majority of an authority's board members shall be citizens residing in the incorporating municipality or incorporating municipalities of the authority.<sup>4</sup>

The choice of board members must also be conditioned by the conflict of interest section of the Municipality Authorities Act. This section prohibits an authority board member from being in any manner interested in any contract or agreement with the authority for any reason.<sup>5</sup> The owner of a business likely to bid on authority contracts does not appear to be the best choice for an appointment to the board. This prohibition has been held to apply only to certain, pecuniary or proprietary interests of the board members. A general interest shared by all residents of the community is not grounds for disqualification.<sup>6</sup>

The eligibility of members of municipal governing bodies to serve on authority boards had been an unsettled issue for some time. However, in 1993, the Pennsylvania Supreme Court determined a township supervisor could legally serve on the board of a municipal authority created by the township.<sup>7</sup> This dual office holding did not violate the Second Class Township Code which limited the appointed offices supervisors could fill,

because authorities are independent agencies of the Commonwealth and not part of the township government. Any incompatibility of office must be established by the legislature, not by the courts. This means that members of county, borough and township governing bodies may be appointed to authority boards. The exception is in third class cities. The Third Class City Code specifically prohibits members of boards of authorities created by the city from serving on city council.<sup>8</sup> The articles of incorporation of an authority may prohibit elected officials from serving on authority boards and these provisions are enforceable in courts.<sup>9</sup>

All authority board members fall within the provisions of the State Ethics Law. They must file the financial disclosure statement required by the Act on an annual basis.<sup>10</sup> Commonwealth Court ruled an elected official violated the State Ethics Law when he voted to appoint himself to an authority board where he received compensation.<sup>11</sup> The State Ethics Commission determined that the Ethics Law did not prohibit a municipal authority board member from simultaneously serving as an employee of the authority and receiving a salary and legitimate reimbursable expenses.<sup>12</sup>

## Board Meetings

**Organization Meeting.** Immediately after receiving the certificate of incorporation, the business of organizing the authority commences. Remember, a municipal authority is an instrumentality of the Commonwealth, not a department of the incorporating municipal government(s). This independent agency coordinates its actions with local government, but it is not controlled by that government. The choice of individuals to serve on the initial authority board is critical, for it is these citizens who set the policies and guidelines under which the authority will operate. In all probability the attorney who serves the municipality, or, in the case of a joint authority, the attorney who serves one or more of the incorporating municipalities, has represented the incorporating local government(s) in the formation of the authority. That attorney will, most likely, be the individual who, in conjunction with all members of the authority board, sets up the first meeting of the authority. The business that must be accomplished at the first meeting of a new authority is extensive, and one of the most critical appointments the authority board must make at that first meeting is appointment of its own solicitor. It is this attorney who will provide the initial guidance to the board members on the powers and limitations on the authority's operation and how the authority can accomplish its purposes to serve the citizens of the incorporating municipality(s). Other critical issues to resolve are the selection of board officers and designation of regular meeting dates.

**Quorum.** A majority of the members constitutes a quorum for the purpose of organizing and conducting business of the board. All action may be taken by a majority vote of the members present, unless the board's bylaws require a larger number in any situation. The board has full authority to manage the properties and business of the authority. It can prescribe, amend and repeal bylaws and rules and regulations. It determines the number and compensation of any employees.

**Attendance.** Unless excused by the board, a member of the authority board who fails to attend three consecutive meetings of the board may be removed by the appointing municipality up to 60 days after the date of the third meeting of the board which the member failed to attend.

**Sunshine Act.** Municipal authority boards are subject to the Sunshine Act. All formal actions and deliberations leading to formal actions must be taken at a duly advertised public meeting.<sup>13</sup> Citizen comments must be heard at meetings prior to the board taking action on issues in front of it. Minutes and records of the board are public documents, subject to the examination of any citizen of Pennsylvania.<sup>14</sup>

**Agenda.** Active authority boards usually meet on a monthly basis. The day-to-day operation of the authority project is delegated to a manager who works within the policy framework set by the board. The board receives reports on the finances and operations of the authority from staff and consultants at its regular meetings. A typical agenda for an authority board meeting includes the following.

- Public comment.
- Approval of minutes of previous meeting.
- Communications from local, state and federal agencies.
- Financial reports, including a summary of revenues, expenditures and balances for all funds for the reporting period and on a year-to-date basis.
- Approval of bills.
- Opening bids.
- Engineer's report, including status of any construction projects.
- Solicitor's report.
- Approval/award of contracts.
- Other old business.
- New business.
- Adjournment.

## **Compensation**

Members of authorities created by school districts may receive no compensation. Members of boards of other authorities may receive salaries as set by the governing body of the appointing municipality. Salaries of board members cannot be increased or diminished by the municipal governing body during the term of a sitting board member. Any salary change will be effective only for subsequently appointed members. Any change in the salary for authority board members must be approved by the governing body of the incorporating municipality.<sup>15</sup>

Authority boards may create positions of officers for the authority, appoint board members to officer positions and set officer salaries. There is no prohibition on board members voting for their own appointments to officer positions or their own salaries as officers.<sup>16</sup> Authority board members participating in a board vote to elect themselves to paid officer positions or to set their salaries as officers do not violate the State Ethics Act. As a matter of good public relations, it might be advisable to refrain from doing this. However, the creation of officer positions specifically to circumvent the requirement of the Municipality Authorities Act that board member salaries be set by municipal governing bodies is an abuse of public office and a violation of the Ethics Act.

Board members may be covered by group life and disability insurance policies. They may not be included in any group coverage for hospital and/or medical benefits. They are not eligible for pensions.<sup>17</sup>

## **Municipality/Authority Relations**

The need for cooperation among the officials of the municipality and the authority board along with the officers, agents and consultants of both entities is absolutely necessary. On the one hand, the municipality must remember the board is composed of qualified and competent citizens, giving of their time, effort, interest and talents toward accomplishing the authority's goals to serve the community. On the other hand, the authority board must realize it is not an entity unto itself. It was created by the municipality to provide a public service. The cost of that service is paid by the property owners within the authority's service area, and those property owners elect the officials who appoint the members of the authority board. Neither the municipality nor the authority can operate effectively within a vacuum. Open communication and willing cooperation between them is necessary to maintain the viability of the public services for the community.

Once an authority is created and its members appointed, a municipality has little direct control over the operations of the authority. The municipal governing body may specify the project or projects to be undertaken by the authority in its original ordinance initiating the incorporation process or by a subsequent ordinance. While the municipality may limit the projects an authority may undertake, it may not limit the powers designated in the Act that may be exercised in carrying out the project. Decisions as to the methods used to accomplish the project are entirely within the power of the authority board. Despite the fact that the authority has full control over the operation of its business affairs, the needs and desires of the municipality as expressed by its elected and appointed officials must be taken into consideration by the board.

**Authority Service Area.** The service area of an authority is a discrete area, typically identified in the articles of incorporation, within which it has the exclusive power to set its rates.<sup>18</sup> Where the articles of incorporation fail to specify a service area, the courts will interpret the service area to be the limits of the incorporating municipality.<sup>19</sup> A municipality may not transfer a portion of an authority's existing service area to another authority. The existing authority is protected by Section 4A(b)(2) of the Act which prohibits the new authority from establishing duplicative or competitive enterprises.<sup>20</sup> However, this section of the Act did not preclude a township from establishing a public water system for a planned residential development which then lacked water service.<sup>21</sup> The service duplication has to be real and not potential, that is the service must be existing already and not just a possibility. Sale of water by one authority to another is governed by contract; the buyer is not within the "service area" of the seller.<sup>22</sup>

**Zoning and Land Use Controls.** A municipal authority's use of its property is subject to the zoning ordinance of the municipality where the property is located.<sup>23</sup> Authority compliance can help cement good working relations between the authority and the municipality. The authority should actively participate in the formulation of any changes to the municipality's comprehensive plan or subdivision and land use ordinance. The ability of a sewer or water authority to extend service is critical to the development of the community. The authority and the municipality must reach agreement on the standards for construction of new water and sewer lines by developers under the subdivision ordinance.

**Assessments.** Assessments against properties benefited by construction of new water or sewer lines can be made by an authority only if it has submitted its plan of construction and costs to the municipality where the project is located prior to construction. The municipal governing body must approve the plan and its estimated cost. The aggregate amount assessed against property owners cannot exceed the cost as approved by the municipality.<sup>24</sup>

In the case of business district authorities, the authority must submit its plan for business improvements and administrative services, the estimated costs and proposed method of assessments for business improvements and charges for administrative services to the municipality where the project is located. The municipality must approve the plan, cost, method of assessment and charges before any assessments or charges can be made.<sup>25</sup>

A municipal authority must have the prior approval of the municipal governing body before designating or joining with other local units in designating an area as a transportation development district.<sup>26</sup> Any assessments to be imposed on properties benefited by the transportation facility projects undertaken for the district must be first approved by the municipal governing body.

**Rates and Charges.** A municipal authority has the power to set its own rates and other charges. The municipality has no role in this process except where authorized by contract between it and the authority. Rates must be uniform and reasonable. The municipal authority has the exclusive authority to set tap-in fees. It is the authority's fee schedule and not the incorporating municipality's which is controlling.<sup>27</sup>

**Services.** The authority also has the sole right to determine the services and improvements required to provide adequate, safe and reasonable service, including extensions. An authority as the successor to a municipal water department is not bound by the municipality's prior service line maintenance policy, but has full power to

make its own determination on maintenance responsibilities in determining its services and setting its rates.<sup>28</sup> Any person, including a municipal government, questioning the reasonableness or uniformity of any authority rate or the adequacy, safety and reasonableness of the authority's services, including extensions, may bring suit in the court of common pleas.<sup>29</sup>

Ordinarily, the amount of control exercised by a municipality over an authority is strictly limited. If municipal officials are unhappy with an authority's operation, they are limited to waiting for the opportunity to appoint persons sympathetic to their viewpoint to the authority board. However, the municipality and the authority can enter into contractual agreements that grant the elected officials additional controls over authority activities. Of course, as its ultimate weapon, the municipality always has the right to take over one or all of an authority's projects after assuming the related indebtedness.

## Public Responsiveness

Over the past ten years there has been a great deal of debate among authority officials, local elected officials and members of the Pennsylvania General Assembly over the adequacy of political accountability of municipal authorities. Allegations have been made that authorities operate without sufficient attention to the needs, wants and complaints of the citizens they serve and tend to act arbitrarily to accomplish their purposes. The authorities respond that all authority board meetings are open to the public, and under the 1998 amendment to the Sunshine Act, the authority board (as well as municipal governing bodies) must hear public comments from those attending the meeting prior to taking official action.

Although once formed, municipal authorities are separate entities substantially free from control by the incorporating local government. They are not entirely free, however, since the board members are appointed by the incorporating local governments and one fifth of the seats become vacant each year. Public opinion thus has an official channel for influencing authority management, but pressure would have to be sustained over several years to be effective. The municipality can also restrict an authority's operations by amending the ordinance enacting the articles of incorporation.

There is no certainty authority boards will be responsive to public opinion. The general record of municipal authority operation in Pennsylvania indicates they are usually responsive to public opinion. It is possible for municipal authorities to disregard the public welfare, but in actual practice very few have done so. The relatively small size of most Pennsylvania municipal authorities and the consequent direct and personal accessibility of board members to the public they serve may help explain their superior record.

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3. *Ambridge Water Authority v. Ambridge Borough*, 13 D.&C.3d 303, at 308, 1980, C.P. Beaver Co.
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25. 53 PA.C.S. 5607d (27); Municipality Authorities Act.
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## IV. Authority Operations

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### Powers of the Authority

The Municipality Authorities Act specifies the rights and powers of the authority and vests them in the authority board. The board exercises these powers through its officers, employees and consultants. They include the following.

1. To exist for 50 years as a corporation.
2. To sue and be sued.
3. To adopt a corporate seal.
4. To acquire, hold, lease and use any property or franchise necessary or desirable for carrying out its purpose, and to sell, lease or dispose of its property at any time.
5. To acquire projects by purchase, lease or otherwise and to construct, improve, maintain, repair and operate projects.
6. To adopt bylaws for the management and regulation of its affairs.
7. To appoint officers, agents and employees, prescribe their duties and fix compensation.
8. To fix, alter, charge and collect reasonable and uniform rates and other charges in its service area and to exclusively determine the services and improvements, including extensions, required to assure adequate, safe and reasonable service.
9. To borrow money and issue notes, bonds and other evidences of indebtedness or obligations of the authority.
10. To make contracts and execute all instruments necessary or convenient for carrying out its business.
11. To borrow money, accept grants from and enter into contracts, leases or other transactions with any federal or state agency, any municipality, school district, corporation or authority.
12. To exercise the power of eminent domain.
13. To pledge or otherwise encumber the revenues or receipts of the authority as security for its obligations.
14. To do anything necessary or convenient for promoting its business and the general welfare of the authority and to carry out its legal powers.
15. To contract with any municipality, corporation or public authority of Pennsylvania or any adjoining state for projects crossing state lines.
16. To enter into contracts to supply water and other services to municipalities not members of the authority and to fix the amount to be paid.
17. To make assessments for sewer or water main construction and to charge tapping fees.
18. To make assessments for business improvements and administrative services.
19. To provide financing for insurance reserves.
20. To finance projects by making loans to nonprofit institutions and local government units.

21. To provide hospital, medical, disability and life insurance benefits and establish pension plans for its employees.
22. To appoint police officers who have the same power as other peace officers within the property of the authority, and to regulate vehicular traffic at airports.

## **Bylaws, Rules and Regulations**

The board must write and adopt bylaws generally describing the management of its affairs and the appointment of officers, agents and employees and prescribe their duties. The bylaws should establish employee policy including hours of work, compensation, benefits, discipline, supervision and other related issues. The bylaws should include regulations on the care and control of property of the authority, handling of finances, accounting system, investments, procurement and insurance.

It is important that authorities adopt by resolution a set of rules, rates and regulations governing the form of service to its customer is on record. The development of such a document provides the board and staff with a mechanism to deal with essentially all questions or challenges that staff may be confronted with in the day to day operation of the authority. The rules and regulations must be in conformance with the Municipality Authorities Act and must be specific so as to remove ambiguities that may occur in the absence of such a document.

For example, the rules and regulations for an operating water authority should generally cover the following areas:

1. The history, service area, definition of terms and the authority's responsibility during periods when interruption of service may occur.
2. The application for service, billing, reasons for service terminations, delinquent bills and customer responsibility.
3. Connection and tapping fees.
4. Cross connections and backflow prevention. This program protects customers from possible contamination from backflow into the distribution system from the customer's side of the meter.
5. The authority's policy regarding the service line from the main in the street to the customer's premises including size of service, type of materials permitted and maintenance responsibility for the customer's portion of the service line.
6. Location and installation of fire hydrants both public and private and conditions of use of operation.
7. Installation of residential, commercial and industrial water meters including the size of meters and the authority's specifications for meter pits as well as the maintenance responsibility for the meters and the meter pit.
8. Water main extensions. The authority should have a policy covering the cost sharing of main extensions requested by customers and developers. The policy should include specific language defining the conditions that must be met by any applicant requesting a main extension, a formula for computing capacity charges, tapping fees, connection charges and the authority's policy on refunds should be clearly spelled out.
9. The authority's schedule of rates.

The above items include most, but not necessarily all subjects to be covered. Each authority is unique and may require specific information not listed above. The important point is that the board and staff must have a set of rules and regulations, a legal basis for decision making when administering the authority's business.



## Authority Employees

The board appoints officers and employees to carry out its instructions regarding the operation of the authority. The board has full power to devise its own administrative framework and hire its own employees. One of the most important decisions of the board is to hire a manager who has the professional expertise to carry out the duties as defined by the Board of Directors. Once hired, it is of critical importance to allow the manager the lead role in hiring employees in conjunction with the Board. It is the board's responsibility to set policy and to require the staff to carry out these policies. Inasmuch as the board has the ultimate fiduciary responsibility for the authority, it is prudent for the board to require staff reports on the entire operation on a monthly basis, or more often in some cases.

Authorities are subject to the Public Employees Relations Act. Terms of collective bargaining agreements entered into under the Act can supersede an authority's otherwise exclusive power to manage its own employees.<sup>1</sup>

The authority may purchase individual or group insurance policies covering life, accidental death and dismemberment and disability income for employees. It may provide hospital and medical insurance benefits. It may establish pension plans for employees or join the Pennsylvania Municipal Retirement System.<sup>2</sup> Authorities are included under the Municipal Pension Plan Funding Standard and Recovery Act.<sup>3</sup> Any authority establishing a pension plan for its employees is subject to the actuarial reporting and minimum funding standards established in the Act.

## Professional Advisors

Authority boards receive assistance from professional advisors during the organization and later phases of an authority's existence. These experts devote a considerable amount of time and energy to the authority's activities. Because of this, they are frequently influential in authority affairs even though they have no official decision making role.

The solicitor serves as the authority's legal advisor in its daily operation. Since these various legal duties necessitate constant contacts with board members, the solicitor often exerts a strong influence on authority business.

An architect or engineer prepares plans for the project and supervises construction. They also make rate studies for sewer, water and other projects.

A bond counsel is employed to supply specialized legal advice and to furnish the authority with a statement its bonds have been legally issued. This statement, called a legal opinion, is necessary before bonds can be marketed. Bond buyers rely on the legal opinions of recognized law firms as evidence the bonds are valid and binding obligations on the authority.

A financial advisor, usually an investment banking house, assists the authority by estimating interest costs, determining an appropriate schedule for the maturity of bonds and preparing the prospectus.

A trustee bank serves the authority by receiving the proceeds of the bond issue and paying the contractors or other parties as directed. It receives current revenues and applies them to appropriate funds as specified in the bond indenture, pays the principal and interest on the bonds when due, and attends to such chores as the destruction of bonds and interest coupons when paid. If surplus funds are available, it may invest them for the authority. It chooses by lot the bonds selected for early redemption or purchases them in the open market if available at less than the current redemption price.

The Municipality Authorities Act requires a certified public accountant to examine the authority books at least once a year. This audit report must be delivered to the local government creating the authority and filed with DCED. A financial statement must be published annually. Because of this close association with authority affairs, the certified public accountant may be an informal advisor on financial and administrative matters.

The architect or engineer, solicitor, bond counsel and investment banker usually serve in the early stages of a project. The local government creating the authority can make these initial appointments.

## Acquiring Facilities

An authority may need certain physical properties to supply its intended services to the public. These facilities may be acquired by grant or purchase from the parent local government, from a private company or the authority may construct them.

An authority has the power to acquire, subject to the limitations of the Act, fee simple title or interest or easement in lands, water and water rights considered necessary for its purposes by purchase or eminent domain proceedings. It cannot condemn property owned or used by the United States, the Commonwealth of Pennsylvania, any political subdivision or another authority. It cannot condemn the property of a public service company, property used for burial places or places of public worship. The authority may exercise eminent domain powers both inside and outside the boundaries of its incorporating local government.<sup>4</sup> An example of the need for such an exercise is right of way for a pipeline from a distant water supply source or a connector to reach a sewage treatment plant along a river. The amount of land to be acquired for a project is a matter within the authority's discretion.<sup>5</sup>

If an authority wishes to purchase or lease property subject to the jurisdiction of the Public Utility Commission, it must first notify its incorporating local government of the terms and conditions of the purchase or lease agreement. Before completing acquisition, the municipal governing body must approve by a two-thirds vote. For joint authorities, a two-thirds vote of the governing body of each parent municipality is required.

## Operating Facilities

An operating authority operates its own facilities. It is responsible for the sale of the service, purchase of supplies, personnel administration and maintenance of the facilities, in addition to financing the project. Professionally trained employees handle the daily affairs of the operation, but responsibility for a great many policy decisions rests with the board. An authority has wide freedom to do anything necessary or convenient for the conduct of its business and is not subject to many of the restrictions found in the municipal codes.<sup>6</sup> It may establish reasonable standards, rules and regulations for operation of its facilities, but may not unduly infringe on the property rights of its customers.<sup>7</sup>

In dealing with personnel and budgetary matters, an authority is free from many of the restraints imposed on municipalities by the Commonwealth, but authorities must adhere to certain procedures in letting contracts. The Act requires all contracts of \$10,000 or more for construction or supplies must be awarded on the basis of competitive bidding after the specifications have been advertised. For authorities, these bidding requirements apply only to construction or supplies. Competitive bidding is not required for a solid waste disposal contract,<sup>8</sup> nor for professional services.<sup>9</sup> The bidding requirements apply only where the authority is a party to the construction contract; when the authority serves merely as a financing conduit for a private, nonprofit corporation such as a hospital, the bidding requirements of the Act do not apply.<sup>10</sup>

In most respects, however, an authority is free to manage its own affairs. An operating authority may contract for the services of a management firm. In this case, the contracting firm supplies the technical ability and is the operating agent in all other respects. This method has the advantage of relieving the board of the detailed problems of management. In return, a fee must be paid to the managing firm.

Operating authorities are found managing natural monopolies such as water supply or sewage disposal where the revenue from the sale of the service can be estimated with considerable accuracy. Joint authorities in these fields are usually operating authorities. Transportation authorities operating mass transit systems are also usually operating authorities.

## **Authority Service Area**

The service area of an authority is a discrete area, typically identified in the articles of incorporation, within which it has the exclusive power to set its rates.<sup>11</sup> Lack of clear definition of the service area can give rise to disputes over the rights or obligations for an authority to serve areas beyond the boundaries of the incorporating municipality. Recent amendments to the Act require further coordination of consent by the host municipality when an authority proposes to require property or conduct projects outside of their incorporating municipality or municipalities. Where the articles of incorporation fail to specify a service area, the courts can interpret the service area to be the limits of the incorporating municipality,<sup>12</sup> or they can refer to some other document such as a county comprehensive plan.<sup>13</sup> A municipality may not transfer a portion of an authority's existing service area to another authority. The existing authority is protected by Section 4A(b)(2) of the Act which prohibits the new authority from establishing duplicative or competitive enterprises.<sup>14</sup> However, this section of the Act did not preclude a township from establishing a public water system for a planned residential development which then lacked water service.<sup>15</sup> The service duplication has to be real and not potential, that is the service must be existing already and not just a possibility. Sale of water by one authority to another is governed by contract; the buyer is not within the "service area" of the seller.<sup>16</sup>

Within the defined service area, no matter how poorly defined, the authority cannot discriminate in access to its services between customers located inside and outside the incorporating municipality's boundaries.<sup>17</sup> The best solution to defining the service area of an authority outside the boundaries of its incorporating municipality is through an intergovernmental agreement between the authority and the municipality to be served. The agreement should include an accurate description of the extraterritorial service area, designation of the authority as the exclusive agent to provide service under the outside municipality's comprehensive plan and/or Act 537 plan, right of the authority to use and open public rights of way, allocation of financial responsibility for needed capacity or system upgrades, right of the authority to set rates and charges by board resolution in place of fixing them by contract and the duration of the agreement. In a case where an authority provided sewer service to an outside developer on a contractual basis, the court required the authority to charge only the fees and charges stipulated in the original 1980 contract rather than those set later by board resolution.<sup>18</sup>

## **Keeping Authorities Competitive**

With competition for local electric and gas utilities and long distance telephone service a reality in Pennsylvania, its citizens are accustomed to look for alternative service providers for one-time monopolies, seeking lower rates or improved services. Services provided by authorities are not subject to direct competition, but local elected officials, business leaders and citizens are well aware that inadequate authority service can be replaced. Authorities, therefore, are competing against potential acquirers of their projects. Authorities must improve the effectiveness of their operations, reengineering to employ the latest in technology. Upgrade of data systems in all phases of the operation will provide management more information and allow staff to work more effectively, resulting in greater productivity, improved service to customers and lower rates for all customers. This can only be achieved by a real commitment from the board and authority management for retraining and continuing education of the staff.

## Legal Liability

Authorities are included within the terms of the Political Subdivision Tort Claims Act.<sup>19</sup> The Act delineates the areas of legal liability and establishes procedures for suits against local government units. Authorities are authorized to purchase liability insurance, employ professional risk managers, pool public liability insurance risks with other local agencies and establish self-insurance programs.<sup>20</sup>

## Financing Authorities

Unlike an operating authority, which is totally responsible for the issuing and paying debt and directly operating the project, a financing or leaseback authority borrows money to finance the construction or acquisition of the project, then leases it back to the municipality to operate. The lease is for a stipulated period of time, usually for the life of the outstanding bonds, and obligates the municipality to pay an amount of rent sufficient to meet authority operating costs and debt service payments. The municipality may pay this rental out of project revenues or other resources.

The lease rental debt of the municipality becomes a general obligation backed by its full faith and credit. If necessary, the municipality may supplement user charge revenues with general revenues, including taxes to make the required payments. The full faith and credit pledge, including the ability to use taxes, in turn, lowers the interest cost of the bond issue. In some cases, municipalities prefer to keep the management of the project in house, drawing on the management resources of the general municipal government. School authorities are all leasebacks since there is no user charge for pupils and the school district is the only suitable operator of the plant. Most parking authorities are leasebacks because of the difficulty of estimating user revenue with sufficient accuracy to make the bonds readily marketable.

Problems may arise in a leaseback arrangement when the user revenues exceed the amount needed by the municipality to operate the system and make the lease rental payments. This can be troubling to those project customers outside of the incorporating municipality. There were a number of cases where the customers outside of the municipality challenged the authority and the municipality, raising the question of Public Utility Commission (PUC) jurisdiction over the establishment of rates for those customers beyond the border of the incorporating municipality. The Supreme Court of Pennsylvania has held that the PUC has jurisdiction over leaseback rates where the project serves other municipalities.

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## V. Authority Projects

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**Operating Authorities.** Authorities fall into two general types, operating and leaseback. An operating authority is totally on its own, selling bonds to finance its projects, operating the project and paying off its debt from project revenues. Municipal officials have no role in operating or paying for the project. Authority personnel operate the project and collect user charges directly. The municipality has no financial liability, either current or capital. On the other side of the picture, the only income available to pay off principal and interest on the authority's bonds is the revenue from the project itself. In August 2001, 1,538 active authorities operated one or more projects. These active authorities operated 1739 total projects.

**Financing Authorities.** The other traditional method of handling authority financing is known as the leaseback. In this approach, the authority is only used for the financing, while the local government operates the project. The authority sells bonds to finance the project and then leases the project to the municipality to operate. The lease is for a period of time equal to the term of the authority bonds and the annual rental is set as an amount sufficient to pay off the debt, principal and interest. The local government operates the project and pays lease rentals out of project revenues. When the lease expires and the bonds are paid off, the authority may return ownership of the project to the local government. The local government has responsibility for operating the project. However, lease rentals to support the bonds are payable out of any revenues of the local government if project revenues are insufficient by themselves. This can include taxes.

Another method of strengthening the revenue support for an authority is the double leaseback or service contract. In this arrangement, the authority operates the project but agrees under long-term contract to the municipality to provide service in return for regular payments calculated to be sufficient to meet operating, administrative and debt service expenses. The project is leased first to the municipality which guarantees payment of the bonds, then leased back to the authority for operation.

All authority involvement in financing buildings for schools and nonprofit institutions is leaseback, because the school board or institution itself is the only suitable operator of the facility. Most parking and public building financing through authorities is leaseback, because the revenues from these projects cannot be estimated with sufficient assurance to produce the necessary degree of investor confidence to minimize interest cost. Sewer and water authority financing is either leaseback or operating, depending on local decisions on the desirability of municipal or authority operation and the possible difference in interest costs in each case. Since 1988, municipal authorities have had the power to finance projects of local governments or nonprofit institutions by making direct loans secured by mortgages or other loan agreements.

**Types of Projects.** Municipal authorities may be created only for purposes specified in the Act. The act lists a great variety of projects an authority may finance, own, operate, or lease. Among the most common are water supply systems, sewage collection and treatment systems, mass transit, parking facilities, airports, solid waste disposal facilities and recreation facilities. Authorities may not construct facilities to supply retail electric power, gas, telephone or cable TV service. However authorities may cogenerate electricity at one or more of their projects and, in so doing, use the power itself or sell it. The act restricts authorities from constructing projects that will burden or interfere with existing businesses by establishing competitive enterprises.

When incorporating an authority, the municipality may designate the type project or projects to be undertaken by the authority. The articles of incorporation of the authority may specify what project(s) the authority has the power to undertake. If the governing body does not specify a project or projects, then the authority has the power to undertake any project authorized by the Act, except authorities created by school districts are restricted to constructing public schools. An authority may be incorporated for one or more of the following purposes.

1. Leasing equipment to local governments.
2. Public buildings, including public schools and court houses; parts of these buildings may be leased to private interests to generate revenue.
3. Public market houses and marketing facilities.
4. Transportation terminals.
5. Bridges, tunnels, highways, parkways and traffic distribution centers.
6. Parking facilities.
7. Airports and all necessary airport facilities.
8. Flood control projects.
9. Parks and recreation facilities, including swimming pools, playgrounds, lakes and low head dams.
10. Sewers collection systems and treatment plants, including facilities for treating industrial wastes.
11. Solid waste disposal facilities including incinerators, landfills or other means.
12. Steam heating plants and distribution systems.
13. Producing and selling steam for industrial use from authority projects.
14. Waterworks, water supply works and water distribution systems.
15. Cogenerating surplus electric power at authority incinerator plants, dams, water supply works, water distribution systems or sewage treatment plants.
16. Hospitals and health centers.
17. Buildings and facilities for private, nonprofit, nonsectarian colleges and universities, state-related universities and community colleges.
18. Mass transit, bus and subway systems.
19. Industrial development projects for new or existing industries.
20. Business improvements and administrative services for commercial districts.
21. Financing insurance reserves.

## **Planning an Authority Project**

This begins when the authority is initially incorporated. If the organization of the authority is not administratively sound there will be significant doubt as to whether a project can be planned, constructed, and operated in an efficient and economical manner. Although the affairs of the authority are within the control of the board, the board members themselves probably will lack the expertise and time needed to successfully plan for a project. Consultants and advisors must be retained by the board to perform the many varied and complex tasks that go into planning a project. Great care must be exercised in choosing these consultants and advisors not the least of which, as stated above, is selection of an attorney to be the authority's solicitor. Thought must also be given to when a staff should be selected and hired. Management of a municipal authority in Pennsylvania demands professionalism; it is becoming more difficult as federal and state regulations and statutes themselves become more demanding. An authority manager who will, initially, also be the project director, should be selected early. This individual, as the authority's direct representative, will need to have significant input into the project planning process. The board should have one and only one individual reporting to it—the manager. The hiring of the rest of the staff should be left to the manager with or without board approval.

The first project undertaken by an authority will require extensive use of outside experts. The authority should not appoint any individual or firm to represent it in any manner whatsoever until a mutually agreeable contract or agreement has been negotiated prior to the appointment. The scope of services and fees to be paid must be among the terms of the contract or agreement. As the authority matures and grows, the authority's staff can perform some of those tasks which, at first, are assigned to appointed consultants. Frequently older and larger authorities can complete all phases of a project using only authority staff personnel.

## Steps for Initiating a Typical Authority Project

Shown below are common events that frequently take place during the planning for an authority project. Not all the events need happen for each and every project, and the events listed need not occur in the order listed. In addition, depending on the type of project, some planning functions that are not listed here may be required.

**Determine Need for Project.** The municipality or municipalities take the lead in determining the need for a project, working through their planning commission, staff and elected officials. Municipal officials further decide that the project will be constructed and operated by a newly formed or existing authority. For the steps involved in incorporating a new authority, see Chapter 2.

**Establish Authority Planning Process.** The authority board consults with its manager, solicitor and/or engineer as to what steps or functions are required and necessary in planning for the project.

**Appoint Project Architect or Engineer.** Following appropriate selection processes an engineer and/or architect is appointed. The authority will need to have a registered, professional engineer or engineering firm on retainer after or before completion of the planned project. This engineer/architect need not be the same engineer/architect who is appointed to design a planned project. It may be in the authority's best interest to retain one engineer/architect to plan a project and a different engineer/architect to design the project. The pros and cons involved in planning and designing projects must be debated and decisions reached as to what is in the best interests of the public to be served. Many medium and large sized authorities have a qualified, registered professional engineer on staff and therefore can complete the planning process in-house. Frequently, in-house personnel also can complete the design process depending on the size, skills and experience of the authority staff.

**Apply for Initial State Approvals.** The appropriate department within the Commonwealth must be consulted at the beginning of the planning process and initial approvals, if required, must be obtained from that department.

**Appoint Bond Counsel and Investment Banker.** A decision must be reached on how the project is to be financed. If bonds are to be sold, the authority will need to appoint a qualified attorney as bond counsel. The need and/or desire to appoint an investment banker should be considered. As an alternative, some authorities retain an investment advisor, on a fee basis, whose job it is to analyze the authority's financial position and then make a recommendation as to how to finance any given project. The authority board, after receiving advice from its solicitor, bond counsel and investment advisor (banker), will choose whether to sell the authority bonds at public sale or in a negotiated, private sale with an investment banker. Either method is legal and there are pros and cons to both. The reputation of the community, the authority, the size and scope of the project and the past performance of the authority in previous projects will affect the method chosen.

**Acquire Site.** For a newly incorporated authority, the authority board will have to make financial arrangements to pay for its consultants' services during the initial planning phases for the project. In addition, in many cases, it will be necessary to acquire a site on which to construct the planned project. In some cases, appropriate land is already owned by the municipality, but often funds for site acquisition must be obtained. Commonly used sources are an advance from the incorporating municipality or a short-term bank loan. Where the initial sums needed are large, pledging the municipality's full faith and credit will be necessary to secure a bridge loan from a bank.



**Initial Engineering Evaluation.** The engineer/architect studies the proposed general concept for the project and then submits an initial evaluation of the project in a report to the authority detailing project requirements, design philosophy, cost estimates and the timetable for project construction. This initial report should contain advice as to what state and/or federal loans or grants are available to the authority for assistance in planning, design and construction.

**Study and Approve Preliminary Plans.** The authority board next approves the engineer's/architect's preliminary or initial plans and authorizes loan or grant application preparation.

**Apply for State Approvals.** The authority must apply for appropriate permits and seek approval from all required state and federal agencies.

**Financial Feasibility Study.** The investment banker studies the financial alternatives, prepares and recommends the most suitable financing arrangements and, along with bond counsel, prepares the prospectus. The authority board must receive and approve the financial studies and prospectus. If bonds are to be sold, the board authorizes the investment banker to prepare the preliminary statement required before offering the bonds for sale.

**Final Plans.** The architect/engineer submits final plans for the project to be approved by board. Once approved, the authority seeks state approvals as applicable based on the actual cost figures. The authority obtains any required permits from the regulatory agencies and directs completion of final design of the project by the engineer/architect. Approval of final design is required and authorization of the bidding process must be directed. The first step is advertising for bids by contractors.

**Receive Contractors' Bids.** The authority receives and opens bids from qualified contractors. After receiving the engineer's/architect's analysis of the bids together with their recommendation of award, the board selects the contractor(s). The total amount of money required to complete the project is calculated after bids are awarded.

**Prepare Bond Sale.** Bond counsel prepares the opinion covering the anticipated bonds to be sold, drafts the trust indenture, oversees preparation of the bonds and works with the authority solicitor in preparing all documentation required in sale of the bonds. Bond counsel, the investment banker and/or financial advisor will advise the authority on the need for bond insurance. The authority board, based on recommendations from its advisors, will decide whether to sell the bonds at a public sale or a negotiated, private sale.

**Grant/Loan Approval.** Federal and/or state loans or grant offers are reviewed and, if desired, approved.

**Settlement for Bonds.** The bid for bonds (if a private sale) is received from the syndicate managed by the investment banker, or the bonds are sold at a public sale. The board appoints a trustee bank (based on proposals previously requested and received), the trust indenture is approved and bonds are printed.

**Sign Contracts.** The board awards construction contracts. Any preconstruction loans or advances from the municipality are repaid from the bond funds. The board decides on a supervising engineer for the construction phase and orders construction to commence

Initiating an authority project is a long, difficult and complex process, and is more so when the project is the first to be undertaken by the board members. It is essential for the board to assume ultimate responsibility for completion of the project. It must keep in mind that advisors have been hired to represent and work for the authority board during the construction phase. The solicitor, bond counsel, engineer, architect, financial advisor (investment banker) and others are there to implement the decisions of the board. The role of the appointed advisors is to advise, not to determine the board's course of action.

## VI. Authority Project Funding

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The method chosen to fund a project undertaken by an authority depends on a number of factors.

- How large is the project?
- How much money does the authority have in reserve for capital projects?
- What kind of reputation does the authority have in the financial markets?
- What kind of reputation does the community have in the financial markets?
- What kind of relationship does the authority enjoy within the banking community?

The answers to all of these questions will help decide how the authority finances its project.

**Project Size.** If the contemplated project is large, say greater than a few million dollars, the authority probably will choose a bond issue to raise the required funds to build its project. Most initial construction projects fall into this category, especially when it is realized, for instance, costs for a new sanitary sewer collection system will be in excess of \$100 per lineal foot.

**Available Reserve Funds.** If the authority has been in business for quite some time and has practiced sound financial management, a portion of the authority's reserve funds may be available to underwrite some, if not all, of the project costs for a relatively small capital project. The authority manager will be able to advise the board on how large a project the authority can handle itself without the need to borrow money. Where reserve monies are insufficient to complete a small project, perhaps a bank loan, negotiated with favorable terms, is the financial vehicle the board should choose.

**Creditworthiness.** If a new water treatment plant, a trash recycling center or an upgrade to the wastewater treatment plant is needed to maintain the quality of life in the community, but the town is run down, local businesses are leaving or are failing, and the authority is having trouble making the mandatory payments to its trustee bank for principal and interest on its existing bonds, then the authority and the community are in trouble. It may be possible to float a bond issue for one of the above listed projects, but the interest rate demanded by investors could be high.

### Initial Funds

Funds for preliminary surveys and other organizational expenses may be supplied by grants or loans from the parent local government or a state or federal agency. The municipal codes allow local governments to make grants and loans to municipal authorities. This is often done where studies must determine the feasibility of a new project, particularly for water and sewer systems. These funds can be repaid when the authority issues bonds.

A newly organized authority may issue short-term notes to cover its initial expenses. In this case, the notes will be repaid after bonds for the project have been sold. Grants from state or federal agencies may defray some of the costs of capital construction. This is an important factor for airport and transit authorities.

## Bonds

Before commencing on the construction of its project, an authority will usually issue bonds. Operating authority bonds pledge solely the prospective revenues from the project. For many authorities across Pennsylvania the revenue and/or assessment bond issue is the vehicle chosen to underwrite the costs to be incurred in building the authority's project. An assessment bond issue is used to partially defray capital costs for providing service to an explicitly defined area.

**Tax Exemption.** If certain financial conditions are met, the interest paid on bonds issued by a Pennsylvania municipal authority is exempt from federal income tax and from Pennsylvania state and local income taxes. Such tax exemptions make this type of investment especially attractive to purchasers in high-income brackets and institutional investors such as insurance companies and large pension plans. Tax-exempt status allows authority bonds to be sold at a rate of interest lower than taxable corporate bonds of equivalent quality.

**Term.** The term for revenue bonds may not exceed 40 years, but often is less than the maximum. The authority may issue serial bonds, with some maturing each year, or term bonds where a group or all of the bonds mature in a specified year. Assessment bonds usually are much shorter in length, typically 5 or 10 years, and are of the term type where all bonds mature at once. The term of the assessment bonds is not longer than the period allowed to property owners to pay the assessments levied against their properties. The assessment bond issue gives an authority an opportunity to partially finance a capital project at a lower rate of interest [the term of the bonds is short, therefore the interest (coupon) rate is lower] than does the revenue bond issue. The lien of assessments levied against properties served by the project is pledged as security for the assessment bonds. Experience has shown that the vast majority of property owners pay their assessments in full and on a timely basis.

**Leaseback Authorities.** The revenue pledged by financing or leaseback authorities is the stream of lease rental payments pledged by the incorporating local government (or nonprofit institution, where applicable). When the authority leases its project to a municipality, the leasing local government pledges its full faith and credit to make the lease rental payments. The total amount of lease rentals payable by the municipality are then included within the total outstanding debt for computing a local government's debt limit. This pledge of the taxing power of the municipality in addition to user revenues makes the authority's bond issue more attractive to investors.

## Trust Indenture

In order to provide security for the bondholders and to make the bonds more attractive to investors, the authority typically enters into a trust indenture with a qualified banking institution. The revenues generated by the authority's user charges are assigned to the trustee bank for administering the terms of the trust indenture and the bonds. The trust indenture lasts as long as bonds are outstanding. It gives bond buyers assurances that authority revenues will be used exactly as required by the indenture.

The typical trust indenture contains many clauses and provisions that control how the authority is financially managed. Requirements for debt service reserve funds, operating and maintenance reserve funds, insurance (and beneficiaries under the insurance policies) are detailed in the trust indenture. The size and experience of the authority will control, to some extent, how tightly the authority's hands are tied in controlling its financial operations. An experienced bond counsel prefers to write tight trust indentures to provide maximum protection for the bond holders, while an experienced authority manager often resists the limitations imposed on the operation of the authority by these restrictive clauses in the trust indenture. A compromise is hammered out while the trust indenture is being drafted. A tighter indenture will reduce the premium for bond insurance and will be a useful selling point when marketing the bonds to investors.

**Coverage.** One of the more restrictive provisions of the typical trust indenture is the requirement that the authority include in its rate structure an additional 10% to 20% above the amount required, on an average annual basis, to service its debt and pay its operating costs. This amount, called coverage, is designed to provide additional protection for the bondholders by ensuring sufficient revenues will be collected to any potential shortfalls in the flow of funds for operating and administrative expenses of the authority together with debt service costs. Operating authorities subsist solely on user charges and these are not considered as reliable as lease rentals paid by tax-levying local governments. Coverage is a safety factor allowing accumulation of a reserve fund available in case of emergencies or unexpected revenue shortfalls, and can be used to redeem bonds early or to expand facilities.

A trust indenture that protects the revenue stream can allow title to the project to be changed. In one case, an authority's trust indenture precluded entering into any contract or taking any action that might diminish the rights of bondholders as long as bonds were outstanding. This did not prevent conveyance of the sewer treatment plant to an areawide authority as long as the court was assured the rights of the bondholders were protected.<sup>1</sup>

## Bond Sales

There are two methods for selling authority bond issues: 1) public sale, or 2) a private sale to an investment banker. Early in its project planning, the authority must decide which type bond sale should be used. This is one of the reasons why a qualified bond counsel is appointed by the authority. The bond counsel advises the authority on the best sale method to use. In either case, a qualified investment advisor or investment banker will recommend a maturity schedule for the bonds, prepare a preliminary and final statement describing the authority, the community, the project and the terms of the proposed bond issue.

**Public Sale.** When public sale is selected, bids are requested by public advertisement. After receiving the bids and, with advice from the investment advisor and/or banker, the authority selects the bidder who has offered the most favorable terms. The majority of bond sales is of the negotiated type. Advertised public sales are most likely to occur when the bond issue is quite large and the authority is well known or information concerning its offering is readily available.

**Private Sale.** When the authority chooses private sale, the investment banker, on the date selected by the authority, submits an offer to buy all the bonds, listing in the proposal the terms of the offer. If the sale is of the public type, the authority will pay a fee to the investment banker for their services. But, if the sale is of the private type, the investment banker earns their fee through the bond discount. The authority does not receive the entire face amount of its issue. The amount of the discount represents the investment banker's fee for taking all the risk in reselling the bonds and for their services during the planning phase of the project. The majority of bond issues are of the private or negotiated type. This method works because information regarding interest costs and other terms of bond sales is widely disseminated. The nation's money market is competitive and results of negotiations are public knowledge. Authority officials can compare an offer with recent sales by similar organizations. Ethical standards among investment bankers are high and the reputation of a house is its chief stock in trade.

## Interest Rates

The interest costs on authority bonds will vary from one year to another and from one authority to another. They may also display a pattern of rates distinct from federal government issues or corporate bonds. Many factors affecting interest costs are beyond the control of the issuing authority or the parent community. Supply and demand for municipal bonds on any given day will have an effect on the interest rate. The current monetary policy of the Federal Reserve System, the fiscal policy of the federal government and the condition of the national economy are other powerful determinants causing the whole array of interest costs to vary over time.

Within the national economy, conditions of a localized nature affect the risk factor and thus the specific bond issue's position in the competitive market. For example, an authority in a chronically depressed area finds its interest costs are higher than its more prosperous neighbor.

The past debt record or reputation of the community is important. Even though the authority is a separate entity and may be borrowing for the first time, it is judged, in part at least, by the debt record of the incorporating municipality and all overlapping governmental jurisdictions, including the county and school district. This is especially true if it is a leaseback authority supported by rentals from a taxing unit. Obviously, this influence operates in the reverse direction as well. Consequently authorities and parent local governments are not as separate entities in economic fact as they are in legal principle.

Size of the bond issue affects interest costs because the unit cost of investigation and preparation decreases as the amount underwritten by an investment bank increases. Time to maturity is still another rate determining factor, with longer terms involving higher risks and higher rates. Longer-term bonds can and do demand a higher rate because risk is greater due to future unknowns in the out years.

Finally, authorities issue revenue-type bonds and this characteristic affects the interest cost. Where the revenue source consists of rentals paid by a tax-levying local government, the risk is approximately the same as that applying to the local government's general obligation bonds. Revenue bonds based on user charges involve higher interest cost since buyers have less confidence in the estimates of authority income. The project type will also have an effect on the interest rate that must be offered. For instance, sewer systems offer a more solid and assured revenue stream than do parking facilities or swimming pools.

## **Bond Redemption**

Authority bonds often are redeemed ahead of schedule when it is in the authority's best financial interests to do so. Sometimes market conditions will allow an authority manager to buy back some of the authority's bonds on the open market at a significant discount.

An entire bond issue, or a significant part of it, may also be redeemed ahead of time or called as a result of refunding if the bond agreement contains such an option. Refunding happens when the pattern of interest rates falls after the authority has issued bonds, or its own credit rating improves and thus causes its position in the market to change. The authority is then able to issue new, lower cost bonds and use the proceeds to redeem the original issue at the premium or penalty included in the agreement.

Authority bonds can also be defeased. In a defeasal, the authority issues new bonds (at a lower interest rate) and deposits the money with a trustee bank which invests it and assumes the responsibility for paying off the original bonds as they come due. This process is useful where the bond agreement does not permit advance redemption of the original issue.

Early bond retirement is also likely to be the result of the coverage or risk factor included in the estimates of revenue needed for debt service purposes. This factor leads to the accumulation of a reserve. It can be used for the early retirement of bonds, either through direct refunding or defeasal. Due to this feature, bond issues usually are fully retired with a ratio of actual to nominal life of approximately four to five.

## **Default**

If an authority fails to pay the interest and principal when due, it is in default. Many failsafe factors have been built into authority financing to prevent default. However, the Municipality Authorities Act does provide remedies to the bondholders in the event of a default or failure of the authority to fulfill any of the covenants in the indenture.

In the event of default on the payment of principal or interest, the trustee can file suit in the court of common pleas to require the authority to collect rates adequate to meet its obligations. The court may appoint a receiver to operate the authority's facilities and to collect the rentals or other revenue. In a leaseback situation, the receiver could bring court action to force the leasing local government to raise the necessary money by rates, charges or taxes to pay the lease rentals. In either case, the projects and other assets of the authority cannot be sold in order to satisfy the creditors. This ability to seize revenue combined with the inability to seize property is the key characteristic of revenue bonds.

Municipal authorities cannot file for bankruptcy under Chapter 9 of the Bankruptcy Code. Federal law requires affirmative action from a state before a public entity can file for bankruptcy. Pennsylvania has no legislation permitting municipal authorities to file.<sup>2</sup>

## **Bank Loans and Other Alternatives**

This chapter concentrates on the sale of bonds to fund an authority project, but there are other vehicles available for financing a capital project. Bank loans are used frequently where the project is relatively small and attractive repayment terms can be negotiated with a bank. Interest earned on a loan to a municipal authority may be tax exempt to the bank if its "qualified" portfolio is within the bounds set by the IRS. If so, the bank may be in a position to offer extremely competitive rates on a loan to the authority. There are a few financing authorities that have sold bonds and used the proceeds to finance capital projects by municipalities and other authorities. The rules and regulations for using this type financing vary from authority to authority. On a case by case basis the bond counsel and/or investment banker can provide information and advice on the availability and appropriateness of these other sources.

## **Government Grants and Loans**

The era of large grants from the federal government to finance authority projects, especially sewer collection and treatment systems, is over. In the late 60's and early 70's it was not unusual for the federal government to underwrite 70% of a sewer project. Those large grants are no longer available, but some grant money is available for water and sewer projects. Pennvest loans and grants to eligible communities can provide needed relief; the authority's engineer can assist with the application. As with all grants and loans there are advantages and disadvantages to using these type vehicles to finance a project. Pennvest representatives can answer any questions or provide detailed information on their programs.

## **Extent of Authority Borrowing**

Municipal authorities have a major presence in the municipal bond market for Pennsylvania local governments. The largest category is authority debt issued to finance construction projects of nonprofit institutions, primarily hospitals, nursing homes and colleges and universities. However, this category has decreased since the issuance of Governmental Accounting Standards Board Statement No. 14 (GASB 14). This standard removes the liability for debt repaid directly by the nonprofit institution from the authority's balance sheet. As more financing authorities have been adopting GASB 14 in the past 7 years, this category of authority debt is declining.

Most of the debt issued by local government facilities financing authorities is for leaseback sewer and water projects operated by the municipalities. This amount counts as part of the debt of the leasing local government unit. Debt of school authorities has dropped precipitously over the last several decades as authority financing has been replaced by direct school district debt.

The largest categories of debt for operating authorities are for sewer and water authorities. The vast bulk of debt of multipurpose authorities represent debt for sewer and water projects as well. Solid waste and parking projects are secondary purposes for authority debt. Airport and transit authorities have very low levels of debt in relation to their revenues and expenditures—they primarily are involved in operating their projects.

## References

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## VII. Authority Finances

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### Authority Revenues

Operating authority revenues can come from charges levied on users of services, investment earnings or from grants. Some, such as sewer authorities, may impose special assessments and collect connection fees. Total revenue must be large enough to defray administrative and debt service costs plus operating and maintenance expenses and coverage.

Revenue problems are minimized in the case of financing authorities that lease back their projects to municipalities. The annual debt service and administrative costs can be estimated with considerable accuracy. The lease rental charge then equals that figure plus a percentage of debt service to care for unforeseen difficulties. The leasing local government may pay the rentals from its tax receipts alone, or it may receive state or federal grants. In some cases, the local government will defray the rental cost in whole or part by levying user charges. The leasing local government may have problems with revenue flows, but the authority does not face any difficulties once the local government has signed the lease. It is becoming more common for nonprofit institution financing authorities to issue debt that is payable directly by the institution. The institution, not the authority is responsible for the debt. The institution merely pays the authority an annual service fee to cover administrative expenses.

### Initial Funds

When an authority is first incorporated it has no funds. Typically the incorporating municipality advances (loans) the authority sufficient money to get started. The magnitude of the loan will vary depending on the effort to be undertaken by the authority. If the credit worthiness of the incorporating municipality is high enough and the reputation of the authority board members is respected, it may be possible to establish a direct line of credit at a local bank so initial operating funds are readily available. The authority, when getting started, will have some significant bills to pay. These responsibilities should encourage the board to move quickly to make arrangements for operating funds.

### Bond Issue Proceeds

Once a project goes into construction, significant funds will be available from the proceeds of the bond issue. This money is held in trust by the trustee bank and only can be disbursed via approved requisitions. Most of it goes for construction costs and repayment of startup loans. But one of the different funds established under the trust indenture will contain money so the authority can meet its administrative and operating expenses.

### Assessments

**Water and Sewer Authorities.** It is common to recover a portion of the construction costs for sewer or water mains by levying municipal assessments against the benefited properties. An authority may assess property owners for all or part of the costs of constructing sewer and water lines. In calculating assessments, the authority may use either the benefits method, the front foot rule or both simultaneously on the same project.<sup>1</sup> Whether the benefits method or the front foot rule is used, an assessment must always be related to the benefits conferred on the property owner.<sup>2</sup> The front foot rule is merely a convenient substitute for the calculation of benefits, usable in an area of uniform lot sizes. Where this method does not fairly reflect the benefits



conferred, it is invalid.<sup>3</sup> There is a presumption properties abutting on the sewer or water line have benefited. This presumption can be rebutted, but the burden of proof is on the property owner.<sup>4</sup> Where the very nature of the use of the property means that it cannot be benefited from the sewer or water line extension, the property owner is not subject to an assessment.<sup>5</sup> The municipal authority may not recover more than the net project costs, after deducting any state or federal assistance, through the assessment process.<sup>6</sup>

Foot-front assessments may be used only after the authority has obtained approval from the municipality where the assessment is to be levied. In order to obtain the approval, the authority must submit the following information to the municipality prior to the start of construction:

- 1) The plan of construction.
- 2) The total estimated cost of the project.
- 3) The total estimated assessable costs of the project.
- 4) The proposed rate per foot-front the authority intends to assess.

The aggregate amount to be assessed against all benefited properties cannot exceed the estimated cost of the project as approved by the municipality.

When the authority employs the benefit method of assessment, the court will establish the amount of each assessment. Neither the foot-front nor the benefit method of assessment negates or prohibits the authority and a property owner from negotiating an agreement on the amount to be assessed against a benefited property.

Assessment income is used to retire assessment bonds if such bonds were issued to finance part of the capital project. If no assessment bonds were issued, assessment income may be used to replenish any reserve funds used to finance the project.

**Business District Authorities.** Business district authorities may also levy assessments. These assessments are levied on all taxable real estate within the designated business improvement district, either on a pro rata basis or in proportion to benefits conferred as determined by viewers. The municipal governing body must have first approved the plan for business improvements and administrative services.

In the case of business improvement authorities, the authority must submit its plan for business improvements and administrative services, the estimated costs and the proposed method of assessments for business improvements, and charges for administrative services to the municipality where the project is located. Following a public hearing, the municipality must approve the plan, costs, method of assessment, and charges before any assessments or charges can be made. These assessments are levied on all taxable real estate within the designated business improvement district. The assessment is determined either on a pro-rata basis or in proportion to the benefits conferred as determined by a board of view. Authorities may assess for provision of administrative services without providing physical business district improvements.<sup>7</sup>

**Transportation Development District.** A municipal authority must have the prior approval of the municipal governing body before designating or joining with other local units in designating an area as a transportation development district. Any assessments to be imposed on properties benefited by the transportation facility projects undertaken for the district must first be approved by the municipal governing body.

## Connection Fees and Tapping Fees

Certain costs may also be charged through to customers in the form of tapping fees or connection fees.<sup>8</sup>

Connection and customer facilities fees are limited to the cost of laterals from the authority main, including installation of a water meter. Connection fees can also cover the cost of setting up an account, inspecting and testing the connection, and any material provided to facilitate the connection. Connection fees cannot exceed

the actual cost of the connection or be based on the average cost of past connections of a similar type or size.<sup>9</sup> Income from connection fees is a direct offset of expenses incurred in inspecting and testing the connection. The income goes directly to the authority's general fund.

Tapping fees are levied by an authority to recover the customer's share of capital costs. They are charged to recover cost associated with the capacity to provide service, the cost of distribution or collection facilities, the cost of special purpose facilities (such as pumping stations or storage tanks), and the cost of reimbursing private persons who originally paid for construction of the facilities. The tapping fee components must be carefully calculated.<sup>10</sup> The fee must be based on actual historical costs, not bid prices. It must exclude interest, financing costs and grants. It must exclude costs of facilities solely serving existing users. Equipment no longer in use must be deducted from the cost basis. Capacity utilization must be calculated on up-to-date figures.

Where developers have built collection systems within developments and/or connectors to sewer mains, authorities can contract for exemption from some or all connection fees for the purchasers of lots within the development. The authority will be bound by the terms of the contract in application of new fees.<sup>11</sup>

## Rates

If authority revenue comes directly from user charges, a problem is encountered since the potential users have the option of varying the quantity of service they purchase. That is, the compulsion to pay a fixed figure characteristic of lease rentals is no longer present. In setting its charges, the authority must estimate the quantity of service it can sell at each of several possible unit rates. If rates are to change, consideration must be given to the effect this will have on the quantity purchased. Authorities could, although they seldom do, consider the rationing effect of high rates as applied to scarce natural resources. Conversely, low rates as an inducement to the public to use a socially desirable service or discount to quantity users to attract industry may be considered. In short, rates are a means of achieving socially desirable objectives as well as a means of defraying expenses. For most operating municipal authorities in Pennsylvania, the theory of rate determination is relatively simple. They are natural monopolies selling a service like water supply or sewage disposal with an inelastic demand. That means there is little change in the quantity purchased as the price increases. Rates can then be determined by dividing the projected number of sales units into the total anticipated expenses, including a safety factor. Price thus equals average cost.

User charges can be levied both to meet operating expenses and to finance construction of a project. Determining the relative share of capital construction costs to be paid from assessments and from rates is a matter within the discretion of the authority.<sup>12</sup>

**Rate Challenges.** Municipal authorities are given sole responsibility for setting their own rates. The reason for this freedom is to assure bond purchasers the authority will be able to generate enough revenue to pay off the bonds sold to construct the project. Authority rates must be reasonable and uniform. The Act establishes the sole method of recourse for any person aggrieved by an authority's rates as appeal to the court of common pleas, regardless of whether the authority is operating inside or outside its incorporating municipality's boundaries.<sup>13</sup>

As a first step aggrieved ratepayers should argue their case before the authority board before taking the case to the court. Frequently ratepayers are successful in convincing the authority board their argument has merit and have been able to achieve rate relief from the board. Court review of authority rates is limited to determining if there has been a manifest and flagrant abuse of discretion or an arbitrary establishment of the rate system.<sup>14</sup> The burden of proving this rests on the challenger. Absent a court finding of abuse of discretion, it cannot alter rates set by the authority or impose other restrictions.

**Classification.** The power of an authority to set rates allows it to reasonably classify and reclassify its customers.<sup>15</sup> Authorities may set different rates for the same type of user within different geographical service areas or for different types of users within the same service area. The rate variation should be based on a cost of service study showing the difference in costs between providing service to the different classes of customers or to the different districts within the authority's service area. While an authority may structure its rate or rates as an inducement to attract industry or to convince the public to use a socially desirable service, it could prove controversial for the authority. The animosity created by doing that, even if it affects only a few of the authority's customers, could outweigh any advantage in such a rate structure. It might be more equitable to commission a cost of service study and establish the rate structure based on that study. The use of a cost of service study should offset a claim of arbitrary establishment of the rate system.

The authority may base the rates on the reasonable value of the availability of service as well as the amount of actual use.<sup>16</sup> The service provided can be defined in unusual ways. An airport authority's annual permit fee for an off-premises car rental business was levied at 10% of gross revenues derived from rentals to passengers picked up at the airport. The court held that the service provided by the authority was the provision of a marketplace from which the car rental business derives a large portion of its customers.<sup>17</sup> The permit fee was a proper method the authority could use to meet its expenses in operation of the airport.

**Contract Sales.** Municipal authorities may contract with other municipalities or authorities or private utilities to provide them service. Examples are the bulk sale of water, the use of a defined transmission capacity through the authority's sanitary sewer lines, the treatment of wastewater delivered to the authority's wastewater treatment facility, or the disposal of solid waste delivered to the authority's facility. The requirement that rates be uniform and reasonable applies only in the area where customers are served directly by an authority's facilities. This limitation does not apply where an authority contracts with another entity outside the service area and the two entities have negotiated the rate.<sup>18</sup> Even where a municipal authority makes contracted sales outside the boundaries of the municipality that created it, it is not subject to the jurisdiction of the Public Utility Commission.<sup>19</sup>

**PUC Jurisdiction.** Municipal authorities and the service they provide including their rate structures whether operating inside the boundaries of the incorporating municipality are not subject to control by the Pennsylvania Public Utilities Commission. This is not the case for municipalities where services are provided to properties outside its boundaries. Nor is it true where authority projects are leased back to a municipality which then establishes the rates. In these instances the rate charged may be subject to PUC approval if challenged.

**Cost of Service Study.** When establishing rates, authorities would be well advised to conduct a cost of service study, which should be done by a consultant with recognized expertise in rate making. This will provide the authority with evidence to support the rates if they are challenged by customers in the courts or in the PUC review process where the PUC has jurisdiction. The criteria for approval of rates for the private sector are rigorous and are based on cost of service studies to a large extent. Authorities that are being challenged on matters of rates can expect the same degree of scrutiny by the courts or the PUC, therefore the need for a cost of service study. This is more likely to occur for large authorities with large volume users. Courts recognize that for most small authorities calculation of rates is based on authority management experience and general cost knowledge. This is usually sufficient because most are never challenged. However, when challenged, the authority's rates must be supported by a formal cost of service analysis.<sup>20</sup> Such cost of service study can use either the "cash needs" or "utility" approach.

## Investment of Authority Funds

The board of directors has the fiduciary responsibility for instituting the necessary financial controls to safeguard all authority funds. The primary areas of control include internal accounting and investment of authority

money. Investment of authority funds is regulated by Section 7.1 of the Municipality Authorities Act. This section specifies the types of investments permitted. The board can invest the general fund and special funds as provided in the Municipality Authorities Act. Authorized types of investment include the following:

1. U.S. Treasury bills.
2. Short-term obligations of the U.S. government and federal agencies.
3. Savings and checking accounts and certificates of deposit in banks, savings and loan associations and credit unions where such funds are insured by the FSLIC, FDIC, and the National Credit Union Share Insurance Fund.
4. General obligation bonds of the federal government, the Commonwealth of Pennsylvania or any state agency, or of any Pennsylvania political subdivision.
5. Shares of mutual funds whose investments are restricted to the above categories.

In addition, the board can invest the authority's sinking funds as authorized for local government units in the Local Government Unit Debt Act, 53 Pa.C.S. 8224.

The board also is able to maximize the return on authority investments by using one or more of the following strategies:

1. Combining money from more than one authority fund in order to purchase a single investment.
2. Join with one or more political subdivisions and municipal authorities for the purchase of a single investment provided that appropriate separate accounting requirements are followed.
3. Permitting assets pledged as collateral to be pooled in accordance with the act of 1971 P.L. 281, No. 72. This act standardizes the procedures for pledging of assets to secure deposits of public funds.

Federal arbitrage regulations must be followed when investing authority funds. This is especially significant when large blocks of funds become available for investment following bond closing. Authority management and the trustee bank must be cautious because violation of the arbitrage regulations can place the tax-exempt status of the authority's bonds at risk.

The board is required to invest authority funds consistent with sound business practice, exercising the standard of prudence applicable to the State Employees' Retirement System at 71 Pa.C.S. 5931(a). To implement these requirements, authorities need to establish a formal investment policy which would include the objectives of preservation of capital, return on investment, and liquidity and diversification. The results of the authority investments can then be monitored against these objectives.

## **Internal Accounting**

Standard fiscal controls and internal financial safeguards used by government and private business need to be practiced by municipal authorities. The Act itself does not stipulate financial safeguards to be followed. In most instances, financial controls are spelled out in the bond indenture. In addition, in order to issue marketable bonds, the authority must have an unqualified audit opinion from its certified public accountant (CPA). This will require the authority to meet governmental generally accepted accounting principles including acceptable measures of internal control. Authority debt is subject to the antifraud provisions of federal and state securities laws, including disclosure requirements on the accounting practices of the authority.

All funds of the authority must be paid to the treasurer and must be deposited in the first instance by the treasurer in a bank or trust company in one or more special accounts. All revenues are deposited in an approved

bank and money is paid out on warrants. Bank accounts must be either insured or secured by a pledge of direct federal, state or municipal obligations.

Operating authorities use enterprise fund governmental accounting. This includes accrual accounting, requires capitalization and depreciation of property, plant and equipment fixed assets, long-term liabilities are recorded within the body of the fund, and any accrued unfunded pension plan liability is disclosed and listed on the balance sheet.

## **Financial Reporting**

Each year authorities must file an annual report of their financial affairs with DCED and the incorporating municipality on Form DCED-CLGS-04 issued by the department. All authorities must have an annual audit by a CPA. The CPA audit must be filed along with the annual report. Authorities must also publish a concise version of their financial statement each year in a newspaper of general circulation in the service area of the authority.

In addition to the above requirements of the act, the board of directors should require monthly reports from the finance director, controller or other individual responsible for the internal accounting of the authority books and records. Such a financial report generally includes the following:

1. A record of checks drawn during the month. The listing of checks should indicate the payee, the amount, and a brief description of the expense item.
2. A listing of bills submitted to the board for approval and ratification.
3. Financial statements which include comparative revenue for the current month and the same month for the previous year, year to date statement of income versus budgeted figures, year to date revenue report showing the variance from the budgeted amount, year to date expense reports by cost center with comparison to budget, and a balance sheet ending with the current month.
4. Report on investment of funds authorized by the board at the previous board meeting.
5. Board ratification of investment of funds made subsequent to the previous board meeting.
6. Recommendation of investments to be made prior to the next board meeting.

If controls similar to the above are implemented and rigorously followed, the board of directors will have performed their duties with due diligence with regard to fiscal matters.

## **Tax Liability**

Authority property is immune from taxation if used for public purposes.<sup>21</sup> This immunity applies to property used by an authority for its stated governmental purposes. In the case of a solid waste authority it included not only the actual landfill, but also the surrounding buffer land that cannot be used for any other purpose under local zoning regulations.<sup>22</sup> If an authority owns real estate used partly for private use, the portion not devoted to public use is subject to real estate tax.<sup>23</sup> In order to qualify for a real estate tax exemption, the property must be actually used for public purposes. A well field undergoing initial development and awaiting regulatory approvals was not actually being used for a public purpose, and there was no certainty it would be so used. It is the present, and not an indefinite prospective use which controls whether the use is a public use exempt from taxation.<sup>24</sup> Interest paid on authority bonds is not subject to federal income tax. Interest on authority bonds is exempt from the state personal income tax and from any local earned income taxes in Pennsylvania.

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3. *Exeter Township Authority v. Elways*, 388 A.2d 1131, 36 Pa.Cmwlt. 530, 1978.
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8. 53 PA.C.S. 5607d (22); Municipality Authorities Act, Section 4B(t); *Pennco Builders, Inc. v. Blair Township Water and Sewer Authority*, 567 A.2d 758, 130 Pa.Cmwlt. 158, 1989; *Life Services, Inc. v. Chalfont-New Britain Township Joint Sewage Authority*, 528 A.2d 1038, 107 Pa.Cmwlt. 484, 1987.
9. *West v. Hampton Township Sanitary Authority*, 661 A.2d 459, Pa.Cmwlt. 1995.
10. *Ibid.*
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14. *Hopewell Township v. Municipal Water Authority of Aliquippa*, 475 A.2d 878, 82 Pa.Cmwlt. 134, at 141, 1982; *South Union Township Sewage Authority v. Kozares*, 320 A.2d 381, 13 Pa.Cmwlt. 325, at 333, 1974.
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16. *Ridgway Township Municipal Authority v. Exotic Metals, Inc.*, 491 A.2d 311, 88 Pa.Cmwlt. 637, at 641, 1985; *Patton-Ferguson Joint Authority v. Hawbaker*, 322 A.2d 783, 14 Pa.Cmwlt. 402, at 407, 1974; *Life Services, Inc.*, supra.
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18. *Township of Aston v. Southwest Delaware County Municipal Authority*, 535 A.2d 725; 112 Pa.Cmwlt. 434, 1988; *Municipal Authority of the City of Monongahela v. Carroll Township Authority*, 555 A.2d 264; 123 Pa.Cmwlt. 615, 1989.
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20. *Allegheny Ludlum Corporation v. Municipal Authority of Westmoreland County*, 659 A.2d 20, Pa.Cmwlt. 1995.
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23. *West View Borough Authority Appeal*, 113 A.2d 307, 381 Pa. 416, at 422, 1955.
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## **VIII. Types of Municipal Authorities**

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### **Economic Development Authorities**

This is the smallest category of authority, both in terms of numbers of projects, total revenues and outstanding debt. These authorities are involved in tourist promotion, economic development promotion, industrial parks and small business incubator projects.

### **Airport Authorities**

Airports are recognized as a critical economic development asset for their communities. Towns without ready access to air travel are at a disadvantage. Airport authorities are operating authorities, either using their own staff or by contracting to a private airport management company. Grants from the federal, state and sometimes local governments provide most of the capital to construct and expand airports. Operating expenses are lowered because the federal government assumes the cost of air traffic control and services such as weather information. Current revenues come from user charges levied on aircraft using the facilities, rental of space for retail outlets, ticket booths, offices and hangars.

### **Parking Authorities**

Many of the operating parking authorities are double leasebacks, or at least have a contract with the municipality or private enterprise to ensure adequate revenue. This close relationship with the municipal government is necessary if bonds are to be sold because, unlike water and sewer systems, parking is not a natural monopoly. User charges are too unpredictable to provide security for a bond issue. This close relationship also reflects recognition of the effect of parking on public concerns such as traffic control and the economic health of the community. Parking authorities are concentrated in the central cities of metropolitan areas and in urban boroughs. Besides the Philadelphia Parking Authority and the Pittsburgh Parking Authority, other large parking authorities are found in Allentown, Bethlehem, Erie, Harrisburg, Lancaster, Reading and Scranton.

### **Transit Authorities**

The two largest transit systems in the state, those in Philadelphia and Pittsburgh, are operated by authorities formed under special legislation and not under the Municipality Authorities Act. The Southeastern Pennsylvania Transportation Authority (SEPTA) services Philadelphia and the Port Authority of Allegheny County (PAT) provides service to Pittsburgh. Mass transit systems can be fixed route bus systems or demand response bus/van systems, or a combination of both. Generally, the more urban the area, the higher percentage of activity is found on fixed routes. Only SEPTA and PAT operate subway and rail systems.

### **Sewer Authorities**

These include multi-purpose authorities with sewer projects. The largest sewer operating authorities are the Allegheny County Sanitary Authority and the Delaware County Regional Water Quality Control Authority.

Sewer authorities sell bonds to finance acquisition of existing systems or for construction, extension or improvement of a system. For sewer operating authorities, current revenues come from charges on the users of the system. The charge frequently is based on the amount of water used and payment is enforced by the ability

to direct the water utility to terminate water service, as well as the right to lien against real estate. In areas with no public water supply, flat rate charges are calculated on average use per dwelling unit.

## **Water Authorities**

These include multi-purpose authorities with water projects, many of which operate both water and sewer systems. In addition, financing water systems for lease back to the municipality is one of the principal activities of the local government facilities financing authorities.

An operating water authority issues bonds to purchase existing facilities or to construct, extend or improve a system. The primary source of revenues is user charges based on metered usage. The cost of constructing or extending water supply lines can be funded, completely or partially, by special assessments against abutting property owners. Tapping fees also help fund water system capital costs.

Water utilities are also operated directly by municipal governments and by privately owned public utilities under PUC regulation. Because of the costs of complying with federal safe drinking water standards, the state Department of Environmental Protection has a program to assist with consolidating small water systems to make upgrading cost effective.

## **Recreation Authorities**

Recreation authorities are formed to fund and/or operate parks, recreation centers, auditoriums, civic centers, stadiums, convention centers, swimming pools and golf courses.

## **Solid Waste Authorities**

Solid waste authorities fund and operate sanitary landfills, incinerators, transfer stations, resource recovery projects and solid waste collection systems. As well as authorities, municipal governments and the private sector are very active in solid waste collection and disposal.

## **Flood Control Authorities**

Flood control authorities fund and operate flood control protection systems. For many years, the Sunbury Municipal Authority operated the only authority of this type. It funded its operations through a graduated fee structure on residential, commercial, and industrial properties within the city.

As a result of the levee-raising project in the Wyoming Valley and problems managing and maintaining an extensive flood protection system, an authority was formed to manage operations and maintenance of this much larger system. The Luzerne County Flood Protection Authority assumed responsibilities previously managed by individual municipalities within the river watershed. This authority is funded through existing governmental revenues without any direct charge to the protected properties.

## **Business District Authorities**

These are generally small authorities that operate within designated business improvement districts within commercial areas, develop a plan for the improvements and administrative services and, with the approval of the municipal governing body, levy assessments to pay their costs.



Administrative costs improve the ability of commercial establishments to serve consumers. They include free or reduced fee parking, transportation subsidies, public relations programs, group advertising and district maintenance and security services. Business improvements are capital improvements designed to make the district more commercially attractive and functional, including sidewalks, street paving, street lighting, parking facilities, trees and plantings, pedestrian walks, sewers, waterlines, rest areas and rehabilitation or clearance of blighted structures.

Transportation improvement authorities operate under the provisions of the Transportation Partnership Act, 53 P.S. 1621, as well as the Municipality Authorities Act. Transportation improvement authorities build transportation improvements and fund them through property assessments, with the prior approval of the elected municipal officials. This allows creation of public-private sector partnerships to fund projects where benefits are restricted to a small area. Various types of transportation improvements, including those related to railroads, mass transit, ports and airports, are authorized, but the existing transportation improvement authority projects all involve highway interchanges, intersections and access roads.

## **Community Facilities Authorities**

These authorities operate the following community facilities: ambulance services, flood control projects, community centers, libraries, markets and museums.

## **School Financing Authorities**

These authorities are formed by school districts to finance construction or repair of public school buildings. The Act limits the powers of authorities formed by school districts to finance public school projects. School authority debt is completely offset by bond fund assets and lease rentals receivable from school districts, resulting in zero net debt. In the 1950s and 1960s, school authorities were the largest type of authority in terms of outstanding debt. However, over the past 30 years the amount of school debt issued by authorities has decreased precipitately as school districts have switched to funding their capital needs through their own direct obligations.

All school authority projects are leased back to the district. The Department of Education must approve the lease as well as construction plans. The school district pays its lease rentals out of current revenues of the school district. Their sources are local taxes and state school subsidies, since there are no user fees for school buildings.

## **Local Government Facility Financing Authorities**

This debt is completely offset by bond fund assets and lease rentals receivable from municipalities, resulting in zero net debt. These authorities borrow funds for the construction of various types of projects that are leased back to municipal governments to operate. This group also includes several authorities operating bond pools that loan funds to outside local governments and an Allegheny County authority financing municipal community development projects within the county. The vast majority of these authorities finance water and sewer projects. Municipalities operate the projects and make lease rental payments from the user fees charged to customers. Other projects include municipal buildings, parking structures and equipment leasing.

## **Nonprofit Institution Financing Authorities**

The debt of these authorities is almost completely offset by bond fund assets and lease rentals receivable from nonprofit institutions. As more financing authorities have been adopting Governmental Accounting Standards Board Statement No. 14 (GASB 14), this category of authority debt is declining. GASB 14 removes the liability for debt repaid directly by the nonprofit institution from the authority's balance sheet. In addition, changes to federal income tax laws have now restricted borrowing for nonprofits to some extent.

Nonprofit institution financing authorities issue debt to finance construction projects of nonprofit institutions. They engage in financing hospitals and nursing homes, community colleges and private nonprofit colleges and universities, and miscellaneous nonprofit institutions.

## **Multipurpose Authorities**

Multipurpose authorities operate and/or finance more than a single category of project. The majority operates two project types, several operate and/or finance three project types, and one authority operates four project types. The Sunbury City Municipal authority operates water, sewer, solid waste, and flood control projects. Operations of both water and sewer systems is the most common combinations for multipurpose authorities.

## IX. Local Authorities Formed Under Special Legislation

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In addition to the Municipality Authorities Act, a number of state laws authorize formation of local authorities of a specialized nature. Many of these are similar to municipal authorities with special added powers or extra restrictions.

### Convention Center/Stadium Authorities

**Pennsylvania Convention Center Authority.** Organized under the Pennsylvania Convention Center Authority Act,<sup>1</sup> this is a mixed state/local authority. It has constructed and operates the Pennsylvania Convention Center Authority in center city Philadelphia and is governed by a nine-member board. Two members are appointed by the governing bodies of the four suburban counties, two are appointed by the Governor from a list of nominees supplied by the legislative leadership, two are appointed by the mayor of Philadelphia, two are appointed by Philadelphia City Council, and these eight members select the ninth member who serves as chairman of the board. The Act authorizes Philadelphia to levy a 6% hotel room rental tax; 1/3 of the revenue from the tax goes to the city tourist promotion agency and 2/3 goes to financial support of the convention center.

**Public Auditorium Authorities.** Public auditorium authorities can be formed by second class counties and second class cities, acting singly or jointly, or by second class A cities and the county in which they are located.<sup>2</sup> They are governed by a five-member board appointed by the county commissioners or by the city mayor, or jointly in the case of a joint authority.

These authorities may acquire, own and operate public auditoriums, including places for large public assemblies, holding conventions, sporting events, musical and dramatic performances and other business, social, cultural, scientific and recreation events. Facilities can include off-street parking. These authorities can also construct structures on adjacent sites for the purpose of generating revenues. They have the power of eminent domain.

Two such authorities have been formed. The Stadium Authority of the City of Pittsburgh constructed Three Rivers Stadium; its operation is managed by a contracted management company. The Public Auditorium Authority of Pittsburgh and Allegheny County constructed the Civic Center and leases it to a private operator. The authority also has a long-term lease on the Lawrence Convention Center from the Pennsylvania Department of General Services. Both facilities are designated regional assets and receive financial support from the Allegheny Regional Asset District, replacing prior city and county subsidies.

Second class counties are authorized to levy a hotel room rental tax not to exceed seven percent. A portion of the receipts from this tax in Allegheny County are used for financial support of the convention center.<sup>3</sup>

**Third Class County Convention Center Authorities.** The Third Class County Convention Center Authority Act authorizes the creation of convention center authorities in third class counties, either by action of the county governing body alone or jointly with the governing body of the county seat.<sup>4</sup> These authorities may build and operate convention centers/arenas, issue bonds to pay for them and pledge their revenues or mortgage real estate as security. They are governed by an appointed 7-member board with overlapping 4-year terms. The governing body of the county appoints 3 members, the governing body of the county seat appoints 3 members and the appointment of the seventh member rotates between both governing bodies. The county governing body is authorized to enact a hotel room rental tax of up to 5%; 80% of the tax receipts go toward support of the authority and the remaining 20% to the tourist promotion agency.<sup>5</sup> Convention center authorities have been formed under this Act in Berks County and Luzerne County.

## Financing Authorities for Allegheny County and Philadelphia

**Allegheny Regional Asset District.** The Allegheny Regional Asset District was created by Act 77 of 1993.<sup>6</sup> The district is designated as a special purpose areawide unit of local government under Article IX, Section 7 of the Pennsylvania Constitution. While not truly an authority in the strictest definition of the term, the district has many of the characteristics of an authority. The governing body of the district is composed of seven members, four appointed by the county commissioners, two by the mayor of Pittsburgh and one by the other six members of the board.

The Allegheny Regional Asset District assumed the traditional role of the county and city in providing support for institutions determined to be regional assets. Regional assets include regional parks, libraries, professional sports facilities and regional cultural facilities. The Act authorizes the county to levy a one percent sales tax. Half the proceeds of this tax are allocated to the district. The board is prohibited from directly operating any regional asset. It contracts with public and private bodies operating the assets, setting performance and financial goals. The district commits operating funds by signing an operating and support agreement with each asset. The district can also underwrite capital expenditures through the negotiation of capital development agreements.

**Pennsylvania Intergovernmental Cooperation Authority.** The Pennsylvania Intergovernmental Cooperation Authority was established by Act 6 of 1991.<sup>7</sup> The authority was created to assist in restoring confidence of the financial community when Philadelphia was facing critical financial problems and threatened with loss of access to financial markets. The governing body of the authority consists of five members appointed by the Governor and leaders of the Pennsylvania General Assembly. The Secretary of the Budget for the Commonwealth and the Director of Finance for the city are ex officio members of the board. The authority borrowed money and issued bonds to assist the city. The city may pledge any available revenues, including tax revenues for repayment of the bonds. Philadelphia has pledged 1.5% of the city's wage tax to pay the authority's bonds. The Act requires the city to develop a financial plan aimed at restoring fiscal health and to submit the plan to the authority for approval. The plan must include the current fiscal year and the next four fiscal years. The Act also authorizes a one percent sales tax for the city. Sales tax revenues replace the diverted wage tax revenues in the city's general fund.

## Housing Authorities

Housing authorities may be created by cities and counties.<sup>8</sup> They are governed by boards of five members appointed by the county commissioners and mayors of third class cities. In second class cities, the mayor appoints seven members. In first class cities, the mayor appoints two members, the city controller appoints two, and these four select an additional member. All serve for five-year terms.

Housing authorities can exercise the power of eminent domain to clear slum areas and to provide safe and sanitary dwellings through new construction or rehabilitation of existing structures. An early court case upheld use of eminent domain for these two purposes as a public use.<sup>9</sup> Housing authorities qualify as local housing agencies for implementing federal housing laws. They receive a variety of federal subsidies.

Housing authorities may issue bonds to be repaid from the revenues of housing projects and state and federal subsidies. The bonds can be backed by a pledge of revenues and mortgages on property owned by an authority.

## Industrial and Commercial Development Authorities

Industrial and commercial development authorities may be created by counties, cities, boroughs or townships.<sup>10</sup> They are governed by a board of at least five members appointed by the governing body of the organizing municipality for five-year terms. They finance, construct and lease projects for industrial or commercial development using tax exempt revenue bonds.

These authorities may issue bonds backed by a pledge of revenues or mortgage of assets. Sale of bonds and construction of a project must be approved in advance by the Secretary of Community and Economic Development.

Authorities are authorized to undertake industrial, specialized or commercial development projects and sponsor disaster relief projects. Industrial projects include pollution control, manufacturing, research and development, warehouse, distribution and headquarters facilities and tourist and recreation complexes. Commercial projects include wholesale, retail and mercantile facilities, office buildings, hotels or motels, shopping centers, department stores and headquarters facilities.

Specialized projects include airports, docks, wharves, mass transit facilities, public parking facilities, intermodal transportation facilities, nursing homes, industrial parks, public utility facilities, energy source conversions, energy producing activities and construction of rail sidings, spurs and branch lines. Disaster relief projects include replacement or repair of structures and equipment of industrial, specialized or commercial enterprises damaged in a federally declared disaster.

## Parking Authorities

Parking authorities can be formed by cities, boroughs and first class townships under the terms of the Parking Authority Law.<sup>11</sup> They are governed by boards of five members, appointed by the city mayor, president of borough council or president of the board of township commissioners for five-year terms. In contrast to authorities organized under the Municipality Authorities Act, parking authority board members may be removed at any time by the appointing official.

Parking authorities can operate off-street parking facilities, either lots or structures. Portions of parking structures may be leased for commercial use. Air space above or ground space below a parking structure may be sold or leased to private interests. Parking authorities may also administer on-street parking regulations for municipalities.

Parking authorities may issue bonds to be secured by a pledge of revenues. They have the power of eminent domain. Public parking spaces created by a parking authority, whether self-operated or leased to others, are exempt from all taxes whether levied as property taxes or excise taxes. However, those portions of structures leased for commercial use lose tax exempt status.<sup>12</sup>

## Port Authorities

**Philadelphia Regional Port Authority.** The Philadelphia Regional Port Authority was established by Act 50 of 1989.<sup>13</sup> The authority includes the City of Philadelphia and Bucks and Delaware counties. The authority is governed by a board of 11 members appointed by the Governor and state legislative leaders. The purpose of the authority is to administer regional port facilities and port-related projects and activities along the Delaware River. The authority assumed the functions, rights, powers, duties and obligations formerly exercised by the Philadelphia Port Corporation. The port authority is expected to promote economic growth and generate employment and tax revenues for the entire Commonwealth.

The authority has the power to fix, alter, charge and collect fees, rates and rentals for port facilities and port-related projects. It also can establish carrier routes and services between port facilities and port terminals, including water routes. The authority may issue bonds secured by its revenues. It has the power of eminent domain.

**Port of Pittsburgh Commission.** The Port of Pittsburgh Commission was established by Act 133 of 1992.<sup>14</sup> The geographic area covered by the commission includes 10 counties in western Pennsylvania. The governing body of the commission consists of 15 members appointed by the Governor and leaders of the Pennsylvania General Assembly. The purpose of the commission is to develop port facilities in the area to enhance commerce and industry. In addition, the commission is to develop and promote recreational facilities in the port district.

The commission has the power to fix, alter, charge and collect fees, rates and rentals for port facilities and port-related projects. It may acquire and construct port facilities, port-related projects and recreational facilities. The commission may issue bonds secured by its revenues. It also has the power of eminent domain.

**Third Class City Port Authorities.** These authorities may be formed by third class cities to own and operate port facilities and equipment.<sup>15</sup> They are governed by a board of 11 members. The Governor and Secretary of Transportation appoint 2 members and the city mayor appoints the remaining 9 members for three-year terms. The Erie-Western Pennsylvania Port Authority has been organized under this act. The port authority may issue bonds secured by a pledge of its revenues. It has the power of eminent domain. It operates port facilities in Erie Harbor.

## Redevelopment Authorities

Redevelopment authorities may be organized by cities and counties.<sup>16</sup> They are governed by a board of five members appointed for a five-year term by the city mayor or the board of county commissioners.

Redevelopment authorities have the power to condemn properties in designated blighted areas under eminent domain, to clear the land and resell it to private interests for redevelopment. Any redevelopment proposal must be approved in advance by the local governing body. Each sale of land within a redevelopment area must also be approved by the governing body.

Authorities may acquire blighted properties located outside a certified redevelopment area. Such properties must be certified to the authority by a blighted property review committee with representation from the governing body, the redevelopment authority, the planning commission and the chief executive officer. A 1988 amendment to the Urban Redevelopment Law authorizes redevelopment authorities to finance the purchase, construction, rehabilitation, demolition or equipping of commercial or industrial development projects or residential housing projects. Redevelopment authorities also may make loans to owners, purchasers or financial institutions for these purposes. These projects are to have a reasonable likelihood of preventing, slowing or reversing the deterioration of a designated area. Redevelopment authorities may issue bonds backed by a pledge of revenues or mortgages of real estate. Redevelopment authorities rely heavily on federal community development block grant funds, now channeled through the city or county, to carry out their projects.

## Residential Finance Authorities

Residential finance authorities may be formed by second class counties.<sup>17</sup> The authority has most of the powers of municipal authorities, but it is specifically authorized to issue mortgage revenue bonds and make residential loans to be serviced by lending institutions or purchase residential loans from lending institutions. It is governed by a board of not fewer than five members appointed by the county commissioners.

Bonds issued by the authority are tax exempt under U.S. Treasury regulations. Proceeds from the bonds can be used to issue below market rate mortgages to qualifying home purchasers.

## Transit Authorities

**Metropolitan Transportation Authorities – SEPTA.** A 1963 act created a transportation authority within metropolitan areas, defined as a county of the first class and all other counties located entirely within or partly within a 20 mile radius of such county.<sup>18</sup> The authority operates a transportation system in the area. It is governed by a board composed of one member appointed by the Governor and two by the commissioners of each county and the mayor of Philadelphia for five-year terms. The Southeastern Pennsylvania Transportation Authority (SEPTA) was formed under this act.

SEPTA operates a mass transit system in Bucks, Chester, Delaware, Montgomery and Philadelphia counties. It includes subways and elevated rapid rail transit lines, commuter railroad services and bus and trolley lines. The authority has the power of eminent domain and it may issue bonds secured by a pledge of revenues or mortgage of properties. The system is funded through farebox receipts and federal, state and local subsidies.

**Second Class County Port Authorities – PAT.** These authorities are formed by second class counties to operate port facilities and transportation systems within the county and in adjacent areas to the extent necessary for an integrated transportation system.<sup>19</sup> They are governed by a board of up to nine members appointed by the county commissioners for five-year terms. In addition, when the transportation system is extended into adjoining counties, a representative may be appointed by each additional county to have a vote only on matters affecting rates and services within that county. The Port Authority of Allegheny County has been organized under this act.

Since 1964, the authority has run a unified mass transit system known as PAT. It includes bus and streetcar lines, a rapid rail transit line and exclusive busways. The system is funded by farebox receipts and federal, state and county subsidies. Operation of port terminal facilities has been assumed by the Port of Pittsburgh Commission and PAT is now a purely transit authority.

## Obsolete County Authority Legislation

**County Authorities.** County authorities may be created by counties of the second class and second class A.<sup>20</sup> They are governed by three-member boards, appointed by the county commissioners for indefinite terms. Projects they are authorized to undertake include: (1) bridges, tunnels, streets, highways, traffic distribution centers, traffic circles and parkways; (2) airports and hangars; (3) recreation grounds and facilities, public parks, swimming pools and dams.

The Allegheny County Authority was formed under the terms of this act to construct and improve public highways, bridges and tunnels with public works funds borrowed from the federal government under the National Industrial Recovery Act. The 1934 decision by the Pennsylvania Supreme Court upholding the constitutionality of this law set a precedent for later cases challenging authorities formed under the Municipality Authorities Act.<sup>21</sup> This authority no longer exists.

**County Water Supply Authorities.** These authorities may be organized by counties to engage exclusively in the function of water supply.<sup>22</sup> This 1957 law was enacted as a supplement to the Municipality Authorities Act. In addition to the articles of incorporation filed under the Municipality Authorities Act, it requires the county board of commissioners to file a resolution stating the authority is formed for the sole purpose of water supply, designating it a county water supply authority.

County water supply authorities have all powers of other municipal authorities, except they cannot engage in any activity other than water supply. They have a term of existence of 75 years, can issue bonds with maturities up to 65 years, and can enter into water supply contracts with municipalities, authorities or public utilities for terms of up to 65 years. No authorities have been formed under this act.

## References

1. 53 P.S. 16201; Pennsylvania Convention Center Authority Act.
2. 53 P.S. 23841; Public Auditorium Authorities Law.
3. 16 P.S. 4970.2; Second Class County Code, Section 1970.2; 53 P.S. 3000.3061.
4. 16 P.S. 13101 to 13124.
5. 16 P.S. 1770.2, 1770.4, 1770.5; County Code, Sections 1770.2, 1770.4, 1770.5.
6. 16 P.S. 6101-B; Second Class County Code, Section 3101-B.
7. 53 P.S. 12720.101; Pennsylvania Intergovernmental Cooperation Authority Act for Cities of the First Class.
8. 35 P.S. 1541; Housing Authorities Law.
9. *Dornan v. Philadelphia Housing Authority*, 200 Atl. 834, 331 Pa. 209, 1938.
10. 73 P.S. 371; Economic Development Financing Law.
11. 53 P.A.C.S. §55; Parking Authority Law.
12. *Public Parking Authority of Pittsburgh v. Board of Property Assessment, Appeals and Review, Allegheny County*, 105 A.2d 165, 377 Pa. 274, 1954; *Price v. Philadelphia Parking Authority*, 221 A.2d 309, 422 Pa. 317, 1966; *City of Pittsburgh v. Public Parking Authority of Pittsburgh*, 314 A.2d 887, 11 Pa.Cmwlth. 442, 1974.
13. 55 P.S. 697.1; 1989 P.L. 291, No. 50.
14. 55 P.S. 698.21; Port of Pittsburgh Commission Act.
15. 55 P.S. 571; Third Class City Port Authority Law.
16. 35 P.S. 1701; Urban Redevelopment Law.
17. 16 P.S. 5201-A; Second Class County Code, Section 2201-A.
18. 74 Pa.C.S. 1701; Pennsylvania Urban Mass Transportation Law, Article III.
19. 55 P.S. 551; Second Class County Port Authority Law.
20. 16 P.S. 12601; 1933 Sp.Sess. P.L. 114, as amended.
21. *Tratner v. Allegheny County Authority*, 173 Atl. 289, 316 Pa. 65, 1934.
22. 16 P.S. 12901; 1957 P.L. 1006.



GENERAL LOCAL GOVERNMENT CODE (53 PA.C.S.) - POWERS AND DUTIES OF  
AUTHORITIES

Act of Dec. 30, 2003, P.L. 404, No. 57

Cl. 53

Session of 2003

No. 2003-57

HB 51

AN ACT

Amending Title 53 (Municipalities Generally) of the Pennsylvania Consolidated Statutes, further providing for powers and duties of authorities.

The General Assembly of the Commonwealth of Pennsylvania hereby enacts as follows:

Section 1. Section 5607(d)(17), (24), (30), (32) and (33) of Title 53 of the Pennsylvania Consolidated Statutes are amended to read:

§ 5607. Purposes and powers.

\* \* \*

(d) Powers.--Every authority may exercise all powers necessary or convenient for the carrying out of the purposes set forth in this section, including, but without limiting the generality of the foregoing, the following rights and powers:

\* \* \*

(17) To do all acts and things necessary or convenient for the promotion of its business and the general welfare of the authority to carry out the powers granted to it by this chapter or other law[.] , **including, but not limited to, the adoption of reasonable rules and regulations that apply to water and sewer lines located on a property owned or leased by a customer and to refer for prosecution as a summary offense any violation dealing with rules and regulations relating to water and sewer lines located on a property owned or leased by a customer. Under this paragraph, an authority established by a county of the second class A which is not a home rule county shall have powers for the inspection and repair of sewer facilities comparable to the powers of health officials under section 3007 of the act of May 1, 1933 (P.L.103, No.69), known as The Second Class Township Code.**

\* \* \*

(24) To charge enumerated fees to property owners who desire to or are required to connect to the authority's sewer or water system. Fees shall be based upon the duly adopted fee schedule which is in effect at the time of payment and shall be payable at the time of application for connection or at a time to which the property owner and the authority agree. In the case of projects to serve existing development, fees shall be payable at a time to be determined by the authority. An authority may require that no capacity be guaranteed for a property owner until the tapping fees have

been paid or secured by other financial security. The fees shall be in addition to any charges assessed against the property in the construction of a sewer or water main by the authority under paragraphs (21) and (22) as well as any other user charges imposed by the authority under paragraph (9) [but] , **except that no reservation of capacity fee or other similar charge shall be imposed or collected from a property owner who has applied for service unless the charge is based on debt and fixed operating expenses. A reservation of capacity fee or other similar charge may not exceed 60% of the average sanitary sewer bill for a residential customer in the same sewer service area for the same billing period. Any authority opting to collect a reservation of capacity fee or other similar charge may not collect the tapping fee until the time as the building permit fee is due. Tapping fees** shall not include costs included in the calculation of [such] **any other fees[.] , assessments, rates or other charges imposed under this act.**

(i) The fees may include any of the following [fee components] if they are separately set forth in a resolution adopted by the authority [to establish these fees]:

(A) Connection fee. [It may] **A connection fee shall** not exceed an amount based upon the actual cost of the connection of the property extending from the authority's main to the property line or curb stop of the property connected. The authority may also base the connection fee upon an average cost for previously installed connections of similar type and size. **Such average cost may be trended to current cost using published cost indexes.** In lieu of payment of the [fees] **fee**, an authority may require the construction [and dedication] of those facilities by the property owner who requested the connection.

(B) Customer facilities fee. [It may] **A customer facilities fee shall** not exceed an amount based upon the actual cost of facilities serving the connected property from the property line or curb stop to the proposed dwelling or building to be served. The fee shall be chargeable only if the authority installs the customer facilities. In lieu of payment of the customer facilities fee, an authority may require the construction of those facilities by the property owner who requests customer facilities. In the case of water service, the fee may include the cost of a water meter and installation if the authority provides or installs the water meter. If the property connected or to be connected with the sewer system of the authority is not equipped with a water meter, the authority may install a meter at its own cost and expense. If the property is supplied with water from the facilities of a public water supply agency, the authority shall not install a meter without the consent and approval of the public water supply agency.

(C) Tapping fee. [It may] **A tapping fee shall** not exceed an amount based upon some or all of the following [fee components if they are] **parts which shall be** separately set forth in the resolution adopted by the authority to establish these fees. In lieu of payment of this fee, an authority may require the construction and dedication of only such capacity, distribution-collection or special purpose facilities necessary to supply service to the property owner or owners.

(I) Capacity part. The [fee may] **capacity part shall** not exceed an amount that is based upon the cost of capacity-related facilities, including, but not limited to, source of supply, treatment, pumping, transmission, trunk, interceptor and outfall mains, storage, sludge treatment or disposal, interconnection or other general system facilities. [Facilities] **Except as specifically provided in this paragraph, such facilities** may include **only** those that provide existing service [or will provide future service]. The cost of [existing] **capacity-related facilities**, excluding facilities contributed to the authority by any person, government or agency, **or portions of facilities paid for with contributions or grants other than tapping fees**, shall be based upon their [replacement cost or upon] historical cost trended to current cost using published cost indexes or upon the historical cost plus interest and other financing fees paid on [bonds] **debt** financing such facilities. [In the case of existing facilities, outstanding] **To the extent that historical cost is not ascertainable, tapping fees may be based upon an engineer's reasonable written estimate of current replacement cost. Such written estimate shall be based upon and include an itemized listing of those components of the actual facilities for which historical cost is not ascertainable. Outstanding** debt related to the facilities shall be subtracted from the cost[, but debt may not be subtracted which is attributable] **except when calculating the initial tapping fee imposed for connection** to facilities exclusively serving new customers. [Under all cost approaches, the cost of capacity-related facilities shall be reduced by the amount of grants or capital contributions which have financed them. The capacity part of the tapping fee per unit of capacity required by the new customer may not exceed the cost of the facilities divided by the design capacity.] **The outstanding debt shall be subtracted for all subsequent revisions of the initial tapping fee where the historical cost has been updated to**

reflect current cost except as specifically provided in this section. For tapping fees or components related to facilities initially serving exclusively new customers, an authority may, no more frequently than annually and without updating the historical cost of or subtracting the outstanding debt related to such facilities, increase such tapping fee by an amount calculated by multiplying the tapping fee by the weighted average interest rate on the debt related to such facilities applicable for the period since the fee was initially established or the last increase of the tapping fee for such facilities. The capacity part of the tapping fee per unit of design capacity of said facilities required by the new customer shall not exceed the total cost of the facilities as described herein divided by the system design capacity of all such facilities. Where the cost of facilities to be constructed or acquired in the future are included in the calculation of the capacity part as permitted herein, the total cost of the facilities shall be divided by the system design capacity plus the additional capacity to be provided by the facilities to be constructed or acquired in the future. An authority may allocate its capacity-related facilities to different sections or districts of its system and may impose additional capacity-related tapping fees on specific groups of existing customers such as commercial and industrial customers in conjunction with additional capacity requirements of those customers. [In the case of] **The cost of** facilities to be constructed or acquired[, the] **in the future that will increase the system design capacity may be included in the calculation of the capacity part, subject to the provisions of clause (VI). The cost of such facilities** shall not exceed their reasonable estimated cost set forth in a duly adopted annual budget or a five-year capital improvement plan[, and the authority in furtherance of the facilities must take any action as follows:] **. The authority shall have taken at least two of the following actions toward construction of the facilities:**

(a) [obtain] **obtained** financing for the facilities;

(b) [enter] **entered** into a contract obligating the authority to construct or pay for the cost of construction of the facilities or its portion thereof in the event that multiple parties are constructing the facilities;

(c) [obtain] **obtained** a permit for the

facilities;

(d) [spend substantial sums or resources in furtherance of the facilities;] **obtained title to or condemned additional real estate upon which the facilities will be constructed;**

(e) [enter] **entered** into a contract obligating the authority to purchase or acquire facilities owned by another;

(f) [prepare] **prepared** an engineering feasibility study specifically related to the facilities, which study recommends the construction of the facilities within a five-year period; [or]

(g) [enter] **entered** into a contract for the design **or construction** of the facilities[.] **or adopted a budget which includes the use of in-house resources for the design or construction of the facilities.**

(II) Distribution or collection part. The [fee] **distribution or collection part** may not exceed an amount based upon the cost of distribution or collection facilities required to provide service, such as mains, hydrants and pumping stations. Facilities may **only** include those that provide existing service [or those that will provide future service]. The cost of [existing] **distribution or collections** facilities, excluding facilities contributed to the authority by any person, government or agency, **or portions of facilities paid for with contributions or grants other than tapping fees,** shall be based upon [their replacement cost or upon] historical cost trended to current cost using published cost indexes or upon the historical cost plus interest and other financing fees paid on [bonds] **debt** financing such facilities. **To the extent that historical cost is not ascertainable, tapping fees may be based upon an engineer's reasonable written estimate of replacement cost. Such written estimate shall be based upon and include an itemized listing of those components of the actual facilities for which historical cost is not ascertainable.** [In

the case of existing facilities, outstanding]

**Outstanding** debt related to the facilities shall be subtracted from the cost[, but debt may not be subtracted which is attributable] **except when calculating the initial tapping fee imposed for connection** to facilities exclusively serving new customers. [In the case of facilities to be constructed or acquired, the cost shall not exceed their reasonable estimated cost. Under all cost approaches, the cost of distribution or collection facilities shall be reduced by the

amount of grants or capital contributions which have financed them.]      **The outstanding debt shall be subtracted for all subsequent revisions of the initial tapping fee where the historical cost has been updated to reflect current cost except as specifically provided in this section. For tapping fees or components related to facilities initially serving exclusively new customers, an authority may, no more frequently than annually and without updating the historical cost of or subtracting the outstanding debt related to such facilities, increase such tapping fee by an amount calculated by multiplying the tapping fee by the weighted average interest rate on the debt related to such facilities applicable for the period since the fee was initially established or the last increase of the tapping fee for such facilities.** The distribution or collection part of the tapping fee per unit of **design capacity of said facilities** required by the new customer [may] **shall** not exceed the cost of the facilities divided by the design capacity. An authority may allocate its distribution-related or collection-related facilities to different sections or districts of its system and may impose additional distribution-related or collection-related tapping fees on specific groups of existing customers such as commercial and industrial customers in conjunction with additional capacity requirements of those customers.

(III) Special purpose part. [Fees]      **A part** for special purpose facilities shall be applicable only to a particular group of customers or for serving a particular purpose or a specific area based upon the cost of the facilities, including, but not limited to, booster pump stations, fire service facilities , **water or sewer mains, pumping stations** and industrial wastewater treatment facilities. [Facilities] **Such facilities** may include **only** those that provide existing service [or those that will provide future service]. The cost of [existing] **special purpose** facilities, excluding facilities contributed to the authority by any person, government or agency, **or portions of facilities paid for with contributions or grants other than tapping fees,** shall be based upon [their replacement cost or upon] historical cost trended to current cost using published cost indexes or upon the historical cost plus interest and other financing fees paid on [bonds] **debt** financing such facilities. [In the case of existing facilities, outstanding] **To the extent that historical cost is not ascertainable, tapping fees may be based upon an engineer's**

reasonable written estimate of current replacement cost. Such written estimate shall be based upon and include an itemized listing of those components of the actual facilities for which historical cost is not ascertainable.

Outstanding debt related to the facilities shall be subtracted from the cost[, but debt may not be subtracted which is attributable] **except when calculating the initial tapping fee imposed for connection** to facilities exclusively serving new customers. [In the case of facilities to be constructed or acquired, the cost shall not exceed their reasonable estimated cost. Under all cost approaches, the cost of special purpose facilities shall be reduced by the amount of grants or capital contributions which have financed such facilities.] **The outstanding debt shall be subtracted for all subsequent revisions of the initial tapping fee where the historical cost has been updated to reflect current cost except as specifically provided in this section. For tapping fees or components related to facilities initially serving exclusively new customers, an authority may, no more frequently than annually and without updating the historical cost of or subtracting the outstanding debt related to such facilities, increase such tapping fee by an amount calculated by multiplying the tapping fee by the weighted average interest rate on the debt related to such facilities applicable for the period since the fee was initially established or the last increase of the tapping fee for such facilities.** The special purpose part of the tapping fee per unit of **design capacity of such special purpose facilities** required by the new customer [may] **shall not exceed the cost of the facilities as described herein divided by the design capacity of the facilities. Where an authority constructs special purpose facilities at its own expense, the design capacity for the facilities may be expressed in terms of the number of equivalent dwelling units to be served by the facilities. In no event shall an authority continue to collect any tapping fee which includes a special purpose part after special purpose part fees have been imposed on the total number of design capacity units used in the original calculation of the special purpose part** .

An authority may allocate its special purpose facilities to different sections or districts of its system and may impose additional special purpose tapping fees on specific groups of existing customers such as commercial and industrial customers in conjunction with additional capacity requirements of those

customers.

(IV) Reimbursement [component. An amount necessary to recapture the allocable portion of facilities in order to reimburse the property owner or owners] **part. The reimbursement part shall only be applicable to the users of certain specific facilities when a fee required to be collected from such users will be reimbursed to the person at whose expense the facilities were constructed as set forth in [paragraphs (31) and (32).] a written agreement between the authority and such person at whose expense such facilities were constructed.**

(V) Calculation of tapping fee [components].

(a) In arriving at the cost to be included in the tapping fee [components], the same cost [may] **shall** not be included in more than one part of the tapping fee.

(b) No tapping fee may be based upon or include the cost of expanding, replacing, updating or upgrading facilities serving **only** existing customers in order to meet stricter efficiency, environmental, regulatory or safety standards or to provide better service to or meet the needs of existing customers.

(c) The cost used in calculating tapping fees shall not include maintenance and operation expenses.

(d) As used in this subclause, "maintenance and operation expenses" are those expenditures made during the useful life of a sewer or water system for labor, materials, utilities, equipment accessories, appurtenances and other items which are necessary to manage and maintain the system capacity and performance and to provide the service for which the system was constructed.

**Costs or expenses to reduce or eliminate groundwater infiltration or inflow may not be included in the cost of facilities used to calculate tapping fees unless these costs or expenses result in an increase in system design capacity.**

(e) Except as otherwise provided for the calculation of a special purpose part, the design capacity required by a new residential customer used in calculating sewer or water tapping fees shall not exceed an amount established by multiplying 65 gallons per capita per day for water capacity, 90 gallons per capita per day for sewer capacity times the average number of persons per household as established by the most recent census data provided by the United States Census Bureau. If an authority service area is entirely



within a municipal boundary for which there is corresponding census data specifying the average number of persons per household, issued by the United States Census Bureau, the average shall be used. If an authority service area is not entirely within a municipal boundary but is entirely within a county or other geographic area within Pennsylvania for which the United States Census Bureau has provided the average number of persons per household, then that average for the county or geographic area shall be used. If an authority service area is not entirely within a municipal, county or other geographic area within Pennsylvania for which the United States Census Bureau has calculated an average number of persons per household, then the Pennsylvania average number of persons per household shall be used as published by the United States Census Bureau. Alternatively, the design capacity required for a new residential customer shall be determined by a study but shall not exceed:

(i) for water capacity, the average residential water consumption per residential customer, or, for sewage capacity, the average residential water consumption per residential customer plus ten percent. The average residential water consumption shall be determined by dividing the total water consumption for all metered residential customers in the authority's service area over at least a 12-consecutive-month period within the most recent five years by the average number of customers during the period; or

(ii) for sewer capacity, the average sewage flow per residential customer determined by a measured sewage flow study. Such study shall be completed in accordance with sound engineering practices within the most recent five years for the lesser of three or all residential subdivisions of more than ten lots which have collection systems in good repair and which connected to the authority's facilities within the most recent five years. The study shall calculate the average sewage flow per residential customer in such developments by measuring actual sewage flows over at least 12 consecutive months at the points where such developments connected to the authority's sewer main.

(iii) All data and other information considered or obtained by an authority in connection with determining capacity under this subsection shall be made available to the public upon request.

(iv) If any person required to pay a tapping fee submits to the authority an opinion from a professional engineer that challenges the validity of the results of the calculation of design capacity required to serve new residential customers prepared under subparagraph (i) or (ii), the authority shall within 30 days obtain a written certification from another professional engineer, who is not an employee of the authority, verifying that the results and the calculations, methodology and measurement were performed in accordance with this title and generally accepted engineering practices. If an authority does not obtain a certification required under this subsection within 30 days of receiving such challenge, the authority may not impose or collect tapping fees based on any such challenged calculations or study until such engineering certification is obtained.

(f) An authority may use lower design capacity requirements and impose lower tapping fees for multifamily residential dwellings than imposed on other types of residential customers.

(VI) Separate accounting for future facility costs. Any portion of tapping fees collected which, based on facilities to be constructed or acquired in the future in accordance with this section, shall be separately accounted for and shall be expended only for that particular facility or a substitute facility accomplishing the same purpose which is commenced within the same period. Such accounting shall include, but not be limited to, the total fees collected as a result of including facilities to be constructed in the future, the source of the fees collected and the amount of fees expended on specific facilities. The proportionate share of tapping fees based upon facilities to be constructed or acquired in the future under this section shall be refunded to the payor of such fees within 90 days of the occurrence of the following:

(a) the authority abandons its plan or a part thereof to construct or acquire a facility or facilities which are the basis for such fee; or

(b) the facilities have not been placed into service within seven years, or, for an authority which provides service to five or more municipalities, the facilities have not been placed into service within 15 years, after adoption of a resolution which imposes tapping fees which are based upon facilities to be constructed or acquired in the future. Any refund of fees held for 15 years shall include interest for the period the money was held.

(VII) Definitions. As used in this clause, the following words and phrases shall have the meanings given to them in this subclause:

"BOD5." The five-day biochemical-oxygen demand.

"Design capacity." For residential customers, the permitted or rated capacity of facilities expressed in million gallons per day. For nonresidential customers, design capacity may also be expressed in pounds of BOD5 per day, pounds of suspended solids per day or any other capacity-defining parameter that is separately and specifically set forth in the permit governing the operation of the system and based upon its original design as modified by those regulatory agencies having jurisdiction over these facilities. Additionally, for separate fire service customers, the permitted or rated capacity of fire service facilities may be expressed in peak flows. The units of measurement used to express design capacity shall be the same units of measurement used to express the system design capacity. Except as otherwise provided for special purpose facilities, design capacity may not be expressed in terms of equivalent dwelling units.

"Outstanding debt." The principal amount outstanding of any bonds, notes, loans or other form of indebtedness used to finance or refinance facilities included in the tapping fee.

"Service line." A water or sewer line that directly connects a single building or structure to a distribution or collection facility.

"System design capacity." The design capacity of the system for which the tapping fee is being calculated which represents the total design capacity of the treatment facility or water sources.

(ii) Every authority charging a tapping, customer facilities or connection fee shall do so **only pursuant to a resolution adopted** at a public meeting of the authority. The authority shall have available for public inspection a detailed itemization of all calculations, clearly showing **the maximum fees allowable for each part**

**of the tapping fee and** the manner in which the fees were determined[.] , **which shall be made a part of any resolution imposing such fees.** A [revised] tapping, customer facilities or connection fee may be **revised and** imposed upon those who subsequently connect to the system[.] , **subject to the provisions and limitations of the act.**

(iii) No authority [may] **shall have the power to** impose a connection fee, customer facilities fee, tapping fee or similar fee except as provided specifically under this section.

(iv) A municipality or municipal authority with available excess sewage capacity, wishing to sell a portion of that capacity to another municipality or municipal authority, may not charge a higher cost for the capacity portion of the tapping fee as the selling entity charges to its customers for the capacity portion of the tapping fee. In turn, the municipality or municipal authority buying this excess capacity may not charge a higher cost for the capacity portion of the tapping fee to its residential customers than that charged to them by the selling entity.

(v) As used in this paragraph, the term "residential customer" shall also include those developing property for residential dwellings that require multiple tapping fee permits. This paragraph shall not be applicable to intermunicipal or interauthority agreements relative to the purchase of excess capacity by an authority or municipality in effect prior to February 20, 2001.

\* \* \*

(30) Where a sewer or water system of an authority is to be extended at the expense of the owner of properties or where the authority otherwise would construct customer facilities referred to in paragraph (24), other than water meter installation, [to allow] a property owner **shall have the right** to construct the extension or install the customer facilities himself or through a subcontractor approved by the authority, which approval shall not be unreasonably withheld. The authority [may] **shall have the right, at its option, to** perform the construction itself only if the authority provides the extension or customer facilities at a lower cost and within the same timetable specified or proposed by the property owner or his approved subcontractor. Construction by the property owner shall be in accordance with an agreement for the extension of the authority's system and plans and specifications approved by the authority and shall be undertaken only pursuant to the existing regulations, requirements, rules and standards of the authority applicable to such construction. Construction shall be subject to inspection by an inspector authorized to approve similar construction and employed by the authority during construction. When a main is to be extended at the expense of the owner of properties, the property owner may be required to deposit with the authority, in advance of construction, the authority's estimated reasonable and necessary cost of

reviewing plans, construction inspections, administrative, legal and engineering services. The authority may require that construction shall not commence until the property owner has posted appropriate financial security in accordance with paragraph (23). The authority may require the property owner to reimburse it for reasonable and necessary expenses it incurred as a result of the extension. If an independent firm is employed for engineering review of the plans and the inspection of improvements, reimbursement for its services shall be reasonable and in accordance with the ordinary and customary fees charged by the independent firm for work performed for similar services in the community. The fees [may] **shall** not exceed the rate **or cost** charged by the independent firm to the authority when fees are not reimbursed or otherwise imposed on applicants. Upon completion of construction, the property owner shall dedicate and the authority shall accept the extension of the authority's system if dedication of facilities and the installation complies with the plans, specifications, regulations of the authority and the agreement. An authority may provide in its regulations those facilities which, having been constructed at the expense of the owner of properties, the authority will **require to be dedicated and which facility or facilities the authority will** accept as a part of its system.

(i) In the event the property owner disputes the amount of any billing in connection with the review of plans, construction inspections, administrative, legal and engineering services, the property owner shall, within 20 working days of the date of billing, notify the authority that the billing is disputed as excessive, unreasonable or unnecessary, in which case the authority shall not delay or disapprove any application or any approval or permit related to the extension or facilities due to the property owner's dispute over the disputed billings unless the property owner has failed to make payment in accordance with the decision rendered under clause (iii) within 30 days after the mailing date of such decision.

(ii) If, within 30 days from the date of billing, the authority and the property owner cannot agree on the amount of billings which are reasonable and necessary, the property owner and authority shall, by mutual agreement, appoint a professional of the same profession or discipline licensed in Pennsylvania to review the billings and make a determination as to the amount of billings which is reasonable and necessary.

(iii) The professional appointed under clause (ii) shall hear evidence and review the documentation as the professional in his or her sole opinion deems necessary and shall render a decision within 60 days of the billing date. The property owner shall be required to pay the entire amount determined in the decision immediately.

(iv) In the event that the authority and property owner cannot agree upon the professional to be appointed

within 30 days of the billing date, the president judge of the court of common pleas of the judicial district in which the municipality is located or, if at the time there is no president judge, the senior active judge then sitting upon application of either party shall appoint a professional, who shall be neither the authority engineer nor any professional who has been retained by or performed services for the authority or the property owner within the preceding five years.

(v) The fee of the appointed professional for determining the reasonable and necessary expenses shall be paid by the applicant if the amount of payment required in the decision is equal to or greater than the original bill. If the amount of payment required in the decision is less than the original bill by \$2,500 or more, the authority shall pay the fee of the professional. If the amount of the payment required in the decision is less than the original bill by \$2,499 or less, the authority and the property owner shall each pay one-half of the fee of the appointed professional.

\* \* \*

[(32) If a sewer system or water system or any part or extension owned by an authority has been constructed at the expense of a private person or corporation, the authority may charge a tapping fee. The authority shall refund the tapping fee or any part of the fee to the person or corporation who paid for the construction of the sewer or water system or any part or extension of it.]

(33) Provisions of paragraphs (30)[,] and (31) [and (32)] shall apply to residential customers in a municipality where the sewer service is being purchased by the municipality or sewer authority from another municipality or sewer authority having excess sewage capacity.

\* \* \*

Section 2. Notwithstanding section 5(1) of this act, this act shall apply immediately to any connection, customer facilities, tapping or similar fees which are increased or initially imposed subsequent to the effective date of this section.

Section 3. Notwithstanding section 5(1) of this act, the mandatory refund provisions of 53 Pa.C.S. § 5607(d)(24)(i)(C)(VI) applicable to tapping fees based upon facilities to be constructed or acquired in the future shall apply to tapping fees collected subsequent to the effective date of this section regardless of when the resolution adopting such tapping fees was adopted.

Section 4. The following shall apply:

(1) The provisions of 53 Pa.C.S. § 5607(d)(24)(i)(C)(I) and (V)(e) shall not apply for a period of 15 years after the effective date of this section to sewer tapping fees imposed by a joint authority having six or more municipal members which is prohibited from implementing any increase in sewer user fees pursuant to the terms of a contract executed prior to January 1, 2003.

(2) The provisions of 53 Pa.C.S. §

5607(d)(24)(i)(C)(V)(e) shall not apply for a period of five years after the date of closing of original financing when an authority, in order to support the construction of new facilities, used original financing which closed on or before July 1, 2003, which has a term of at least 15 years and in which tapping fees were relied upon to support the debt service on the financing.

Section 5. This act shall take effect as follows:

(1) The amendment of 53 Pa.C.S. § 5607(d)(24), (30), (32) and (33) shall take effect in 18 months.

(2) The remainder of this act shall take effect immediately.

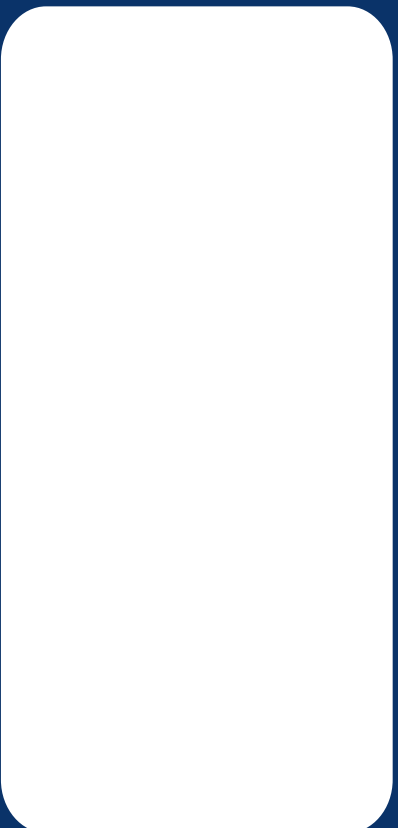
APPROVED--The 30th day of December, A. D. 2003.

EDWARD G. RENDELL

**Pennsylvania Department of Community & Economic Development  
Governor's Center for Local Government Services**

Commonwealth Keystone Building  
400 North Street, 4th Floor  
Harrisburg, PA 17120-0225

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