

IN THE COMMONWEALTH COURT OF PENNSYLVANIA

Dennis M. Davin, in his capacity as
Secretary of the Department of
Community and Economic
Development

Petitioner,

v.

City of Chester

Respondent.

No. 336 MD 2020

Receiver for the City of Chester Status Update

Pursuant to the Court's January 25, 2021 Order (the "January Order"), the Receiver for the City of Chester (the "Receiver") files this Status Update. In the January Order, the Court ordered the Receiver to "file a status report setting forth the progress with implementation and modification of the current Recovery Plan, including information gathering efforts, by or before February 22, 2021."

In this Status Update, the Receiver will update the Court on the City of Chester's (the "City's") financial situation and outline current efforts to implement the Recovery Plan. We are advancing several critical Plan initiatives simultaneously, and much of this update describes those efforts. First, however, we need to highlight the scope of the rebuilding effort necessary to put the City on the path to sustainable financial recovery.

Since filing the first Recovery Plan in August 2020, we have identified several gaps in basic financial management tools:

- The City did not have updated organizational charts for most of its departments, which means there was not a clear, concise way to answer basic questions about chain of

command. Working with the City, we have created those organizational charts and included them in our 2021 budget narrative.

- The City does not have consolidated collective bargaining agreements for its police and fire unions, nor does it have adequate policies to govern compensation for non-represented employees. Instead it has a collection of arbitration awards, side letters and other documents that make it difficult to answer basic questions about employee compensation, to determine if those contracts are being correctly followed, or to conduct labor negotiations. Working with the City, we are in the process of creating those consolidated agreements.
- The City's current financial management software is nearing the end of its useful life. The software provider has informed Chester that it will stop providing customer service on this package later this year. In other words, the software that the City uses to manage every financial transaction and to support basic functions in code enforcement and human resources will gradually become obsolete. Working with the Finance staff, we are in the process of replacing that software.
- The City's computer hardware was also at the end of its useful life. According to the vendor who provides information technology support, the hardware was so old that it was incapable of running current versions of basic office software, incapable of receiving security or anti-virus updates, and ill-suited to accommodate the periods when employees need to work from home for safety reasons. The City replaced that hardware at the end of last year.
- In conjunction with the budget process, the City adopts a salary ordinance that lists each position in City government and its base salary. By reviewing the biweekly payroll runs

for 2021, we found several discrepancies in the salary ordinance, which then impacts the accuracy of the budget. Some discrepancies carried over to the payroll system so that employees were at risk to receive more or less in their biweekly paychecks than they should. Working with City Finance staff, we are correcting those errors.

- The City's most recent comprehensive annual financial report (i.e. year-end audit) covers its performance in 2017. City Finance and the external auditor are working on the 2018 audit, and then they will move on to 2019. The lack of completed audits means that we are operating without a final, clean set of financial data for the two years before the pandemic hit, which would be a valuable reference point for making multi-year projections.

The City's Finance and other senior staff have been forthcoming about these gaps and helpful in filling them. But the absence of these tools makes it harder to identify problems and move on to the primary goal of fixing them.

This list is also only focused on the gaps in basic financial management tools. As we discussed in the November and December updates to the Court, there are similar deficiencies in operations and very basic infrastructure needs. While we were writing this update, we were confronted with the question how to repair a significant leak at City Hall exacerbated by the frequent snowstorms.

We provide this context to the Court because the challenges we encounter every week reinforce a simple truth -- Chester needs to walk before it can run. Part of the process for developing and implementing a long-term plan for the City necessitates fixing the functional issues that are plaguing the City currently and have been for years. For the foreseeable future, we will have to split our time between rebuilding or improving basic daily functions; addressing

time-sensitive financial, operational or litigation issues; and advancing the initiatives that are critical to Chester's long-term recovery.

The City has already made significant progress since entering receivership last year, but that progress will not be linear. In many cases, the City will take two steps forward and one step back. In some cases, Chester will take one step forward and two steps back. But we remain committed to Chester's recovery.

2020 and 2021 Cash Flow Management

One very basic function where we can report progress is paying vendors for the materials, goods and services that they provide to City government. As described in the Recovery Plan, the City carried \$4.0 million in past due obligations from 2019 into 2020 which made cash flow management in the middle of a pandemic even more challenging. Working with City Finance, we believe that the City was able to pay all its vendors before the end of 2020, except where there is an ongoing dispute, while still finishing the year with cash on hand.

We understand that simply paying bills when due is not usually an event that requires acknowledgement. Plus, the City was only able to meet these immediate obligations because it did not make its full annual contribution to the employee pension plans last year, and it furloughed much of its non-public safety workforce for part of the year. But the City was able to make it through 2020 without running out of cash, which was not a given when the fiscal emergency began last year.

Resolution of the 2021 budget

This year's budget builds on last year's modest, but important, progress by funding all obligations to sustain vital and necessary services during 2021 and making the full Minimum Municipal Obligation (MMO) payment to all three pension plans.

Making the full MMO payment is a matter of course for most Pennsylvania governments, even those in Act 47 oversight. Doing so in Chester and halting the now seven-year streak in which Chester has failed to make the full MMO payment will take a focused effort, especially during a pandemic when the speed and degree of economic recovery is unknown.

With the Court's assistance to clarify the Receiver's powers, the Receiver and City elected officials reached an agreement for the 2021 budget which City Council passed unanimously on December 30, 2020 that does the following:

- Implements a 1% distressed pension earned income tax on City residents to achieve compliance with Act 205;
- Increases employee contributions toward the cost of their health insurance, first for non-union employees and then for union employees as new collective bargaining agreements are put in place;
- Consolidates staff from two departments into one Department of Public Works;
- Consolidates staff from the Bureau of Health and Division of Licenses and Inspections; and
- Establishes the Chief Operating Officer position and fills the position on an interim basis.

Adopting a balanced, realistic budget is another step toward restoring financial stability. Staying on budget – monitoring revenue collection, managing any position vacancies, paying bills when they are due, and making careful decisions on discretionary spending – will take focus, discipline and effort throughout the year. It will also require adhering to Plan provisions and to directives made by the Receiver within his powers under the Plan and contained in Act 47.

For example, we identified three employees in the first payroll run of 2021 whose positions the Receiver and the City agreed to eliminate as part of the budget negotiations effective January 1, 2021. We raised their status in subsequent correspondence with City senior and Finance staff and elected officials and even issued a formal directive to immediately terminate these employees on January 28th, but the City continued to employ and pay these individuals through February 10th, despite there being no budgetary authorization to pay them for positions that no longer exist. The City's CFO reported that these individuals were terminated on February 10th.

Setting aside the questions this raises from the perspective of compliance with the Council-adopted budget, the Court-approved Recovery Plan and this Court's ruling that the Receiver can direct the hiring and firing of individual employees, there is the practical matter that the City does not have the money to spend in this manner. Such actions, which run contrary to the Plan and which require the Receiver's team to spend time to address, will prolong the City's recovery in adverse circumstances.

Looking Beyond 2021

While we cannot take the City's cash flow or budgetary position for granted, we also must start to look beyond 2021 at the City's ability to match recurring revenues with recurring expenditures on an ongoing basis and make progress toward the three Rs we laid out in our November update – reducing retiree health care and pension costs; restructuring City operations; and reinvesting in City services.

The updated Plan we submit in April will include a multi-year projection of the City's revenues and expenditures in the General Fund that will undoubtedly show a structural deficit. That analysis, which we expect to update and refine continuously, will guide our strategy going forward.

Reducing health care and pension liabilities

- Based on our current cash flow projections, we do not expect the police pension fund to run out of money in 2021, though its financial condition is still extremely critical. As part of the 2021 budget, the City has budgeted the full MMO payments and has properly implemented the distressed pension tax with those monies dedicated to the pension funds in compliance with Act 205.
- Under the police collective bargaining agreement, the police pension fund is entitled to receive an offset for income earned by police officers who retired on a service-connected disability that they did not have at the time he or she retired. (Note that most of these individuals received a pension benefit equal to 100% of their final salary which is unusual and significantly greater than the 50% required under the Third Class City Code). The agreement requires these retirees to submit to the City's

Controller's Office by April 30th "documentation as to all aspects of earnings, if any, received in the preceding year including but not limited to names and addresses of employers, type of work performed, and copies of federal, state and local tax returns."

If the retiree does not comply with this requirement, the agreement states that the retiree's pension check will be held until he or she complies. The Receiver understands that retirees have not regularly submitted this required tax information to determine any offsets and is working with the City to not only ensure that these submissions to determine offsets occur going forward but also to look back over the last four years to see if any offsets were due.

- The Receiver's team continues to work with the City to transition retirees from the City's health care plans to a Medicare supplemental plan. As of today, 103 individuals have transitioned. Because the City is self-insured for health care, it is difficult to determine the exact savings to the City (since under a self-insured arrangement, the City only pays when covered individuals incur health care costs), but the Receiver's team is closely monitoring City health costs in 2021. The current cost savings estimate is approximately \$850,000 annually. The City FOP leadership has been extremely helpful in this transition.

Restructure City operations

- Eligibility audit: To ensure that only eligible individuals are receiving health care from the City, the Receiver's team is working to contract with a third-party company to conduct a thorough eligibility audit for City-paid health care for both retired and active employees. The Receiver expects the third-party to conduct the audit in the second quarter of 2021.

- Fire study: The City has contracted with McGrath Consulting to study the City's fire department operations. That study has recently begun. DCED is funding the study.
- The Receiver's team has also begun negotiations with the City's Teamster union whose contract expired on December 31, 2020, and preliminary conversations (not bargaining) with its police and fire unions whose contracts expire on December 31, 2021. The Receiver expects to include workforce-related initiatives in the Amended Recovery Plan.

Reinvesting in the City

The Recovery Plan approved by the Court in October included a section on asset monetization, which is integral to generating funding that can be reinvested in Chester's neighborhoods and economy-supporting infrastructure. One of the assets identified for further review is Chester's parking system.

During the September 8, 2020 hearing on the Receiver's proposed Plan, the Receiver's team explained to the Court that we were trying to learn more about the parking contract to determine the best way to proceed including potentially unwinding it. (See Transcript of September 8, 2020 hearing, pp. 109-110). Since that time, the Receiver's team has investigated this matter and determined that it is in the best interests of the City for the Receiver to terminate the parking contract pursuant to the powers granted to the Receiver under section 706 of Act 47. The following is an explanation of the background of the contract and the Receiver's reasoning for his decision.

On April 25, 2018, the City and PFS VII LLC (the "Manager") entered a contract by which the Manager agreed to finance, construct and install equipment and improvements to

manage City parking assets. The City would receive a portion of the profits. On September 5, 2018, the agreement was amended.

The agreement called for 1,500 meters concentrated in three geographic areas of the City including approximately 500 on Widener University's campus. The Manager would finance and construct the parking meters and system and would operate it for 10 years at which point the City would permanently own the parking assets.

The City would receive an "advance" of \$1 million once the 1,500 meters were installed – \$300,000 initially and an additional \$350,000 at 1,000 and 1,500 meters respectively. Additionally, once the 1,500 meters were installed, the City would annually receive a percentage of the annual meter revenue and associated fees after the Manager's costs were covered. The fee sharing schedule as was follows:

- Year 1 (first 12 full months of operations after Commencement Date): 0% to City
- Year 2: 10% to City
- Year 3: 20% to City
- Year 4: 30% to City
- Year 5: 40% to City
- Year 6: 50% to City
- Year 7: 50% to City
- Year 8: 50% to City
- Year 9: 50% to City
- Year 10: 50% to City

The Manager did not guarantee a minimum annual revenue amount to the City, nor were the Manager's costs clearly defined in the contract. Furthermore, there was no cap on the Manager's costs. To date, because of the litigation discussed below, the City has only received

the initial advance payment of \$300,000 as well as some money from rent payments for the Manager's use of an office in City Hall.

The agreement also included a \$12,120,000 payment from the City, referred to as a Default Premium Payment in Exhibit E of the agreement, if the City were to notify the Manager that it intended to terminate the agreement. We understand that there was considerable opposition within the City to agreeing to the terms of this parking agreement.

As of this moment, the Manager has installed approximately 750 parking meters. The Manager has also placed poles for parking meters on the Widener campus and has placed signs in certain neighborhoods for residential permit parking. The Manager is currently collecting parking ticket and parking meter revenue.

On January 2, 2019, Widener University ("Widener") filed a Petition for Preliminary Injunction and Complaint in Trespass against the City and the Manager with the Delaware County Court of Common Pleas seeking to stop meters from being installed on its campus. The case was assigned to Judge Dozer.

On January 9, 2019, Judge Dozer issued a temporary preliminary injunction order finding immediate and irreparable harm to Widener. On November 4, 2020, after a hearing in which Judge Dozer asked if the Receiver would intervene, the Receiver sent a letter to Judge Dozer indicating that he was closely following the litigation and that at that time he did not see a need to formally intervene in the litigation as a separate party. On December 18, 2020, Judge Dozer issued an order giving the Receiver until February 16, 2021, to advise whether he would intervene in this action and if so, providing an additional 30 days to do so.

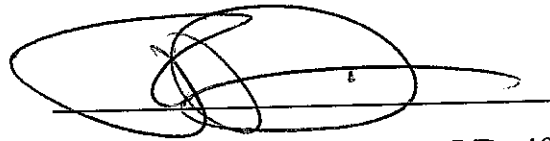
The Receiver's Chief of Staff has spoken numerous times with the parties to better understand the contract and their respective positions in the litigation. The Receiver's team has independently analyzed the terms of the parking contract and determined that it was in the best interests of the City to intervene in the litigation in order to utilize the full powers of the Receiver under the law, including but not limited to Section 706(a) including seeking to "renegotiate, modify, disapprove or terminate contracts and agreements" with the City. 53 P.S. Section 11701.706. We remain available to discuss this matter further with the Court if the Court deems it appropriate.

On February 15th, the Receiver notified PFS VII, LLC of his decision. On February 16th, counsel for the Receiver notified Judge Dozer of his decision. The Receiver has 30 days from February 16th to file his petition to intervene.

Conclusion

The Receiver will continue to provide the Court with ongoing status updates and will provide with Court with any additional information that it requests.

Respectfully submitted,

A handwritten signature in black ink, appearing to be "John P. McLaughlin", is written over a horizontal line. The signature is enclosed within a large, hand-drawn oval.

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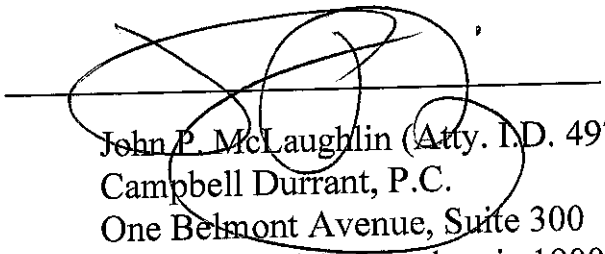
Dated: February 22, 2021

PROOF OF SERVICE

I, John P. McLaughlin, hereby certify that I am this day serving the foregoing document upon the persons below via first class mail, which service satisfies the requirements of Pa.R.A.P. 121:

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Dated: February 22, 2021