

# Chester: Three Years After Fiscal Emergency Declaration & What Comes Next

MFRAC Meeting  
April 11, 2023

# Today's Presentation

- Two days from today (April 13, 2023) will mark the three-year anniversary of Governor Wolf declaring Chester to be in a fiscal emergency.
- The City is quickly running out of time to find and implement a comprehensive solution. If a comprehensive solution is not found by the end of the year, there may be no alternative for Chester but disincorporation.
  - The presentation will explain what disincorporation means, but essentially Chester would cease to exist as a city, would not have any municipal elected officials, and instead would be an unincorporated service district.
  - Ongoing litigation by certain City elected officials in both the bankruptcy matter and the plan modification matter is preventing the Receiver from implementing actions necessary to fix Chester's problems.

# Presentation Outline

- Chester's Financial Condition
- Status of Bankruptcy and Plan Modification Litigation
- Disincorporation

# Chester's Financial Condition

# Chester's Financial Condition

## *Overview*

- The 2019 audit showed a general fund loss of approximately \$6.8 million in 2019 and a cumulative general fund balance of negative \$27.7 million.
- Without an agreement brokered by the City's bankruptcy conflict counsel, the City would have likely run out of money this September.
  - The City's projected year-end general fund balance even with the agreement, although positive, is still critically low.
- A relative "bright spot" is police pension plan funding which has increased from \$1.28 million in July 2020 when the Receiver began work to approximately \$7.77 million in March 2023. The number of months of benefits left in the police pension fund improved from 3 in July 2020 to 16 in March 2023.
- Although the next set of five-year projections has not yet been finalized, the City is still on pace to face an insurmountable deficit in 2025 absent a real solution.
  - Any comprehensive solution will likely take a year to implement. Therefore, the solution needs to be found by the end of this year.

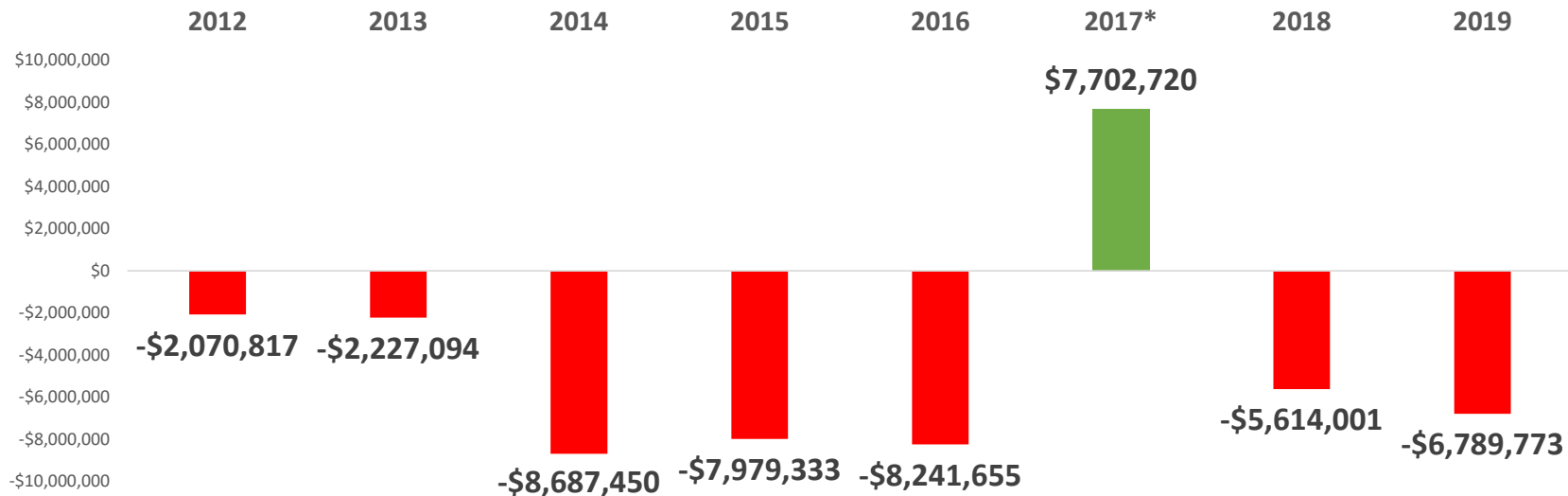
# Chester's Financial Condition

- The City recently released its 2019 audit (work is beginning on 2020) which showed a general fund loss of approximately \$6.8 million in 2019 resulting in the year-end general fund balance of approximately negative \$27.7 million.
  - Note: These amounts do NOT include the approximately \$39.8 million in missed annual pension payments and interest to the City's pension funds (called minimum municipal obligations or MMOs)
- The 2019 general fund loss was the seventh annual loss in eight years. The only year without a loss came as a result of the City borrowing money to pay its bills in 2017.
- This continued trend of significant general fund losses (even with skipping full payments into City pension funds occurring prior to Receivership) clearly shows the City's inability to balance its budget. Though we do not have audits for 2020-2022, we also expect to see large general fund losses for those years as well.

# City Annual General Fund Results 2012-2019

The City's 2019 audit showed a \$6,789,733 loss in the City's general fund. This value is equal to 13.7% of 2019 general fund revenues, which is significant.

**Audited City General Fund Results 2012-2019**

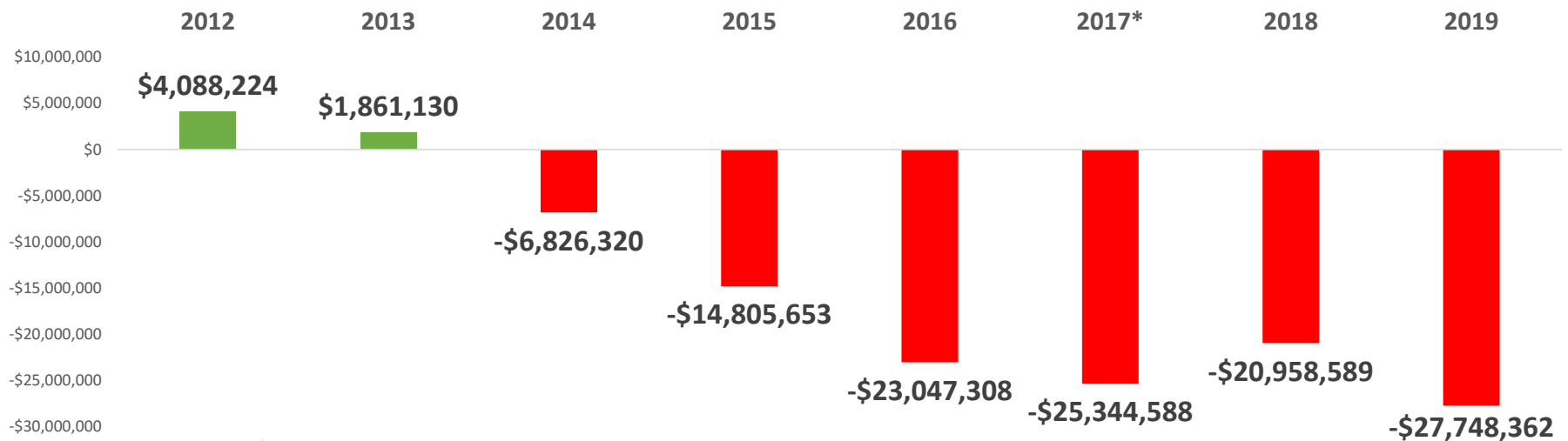


\*Note: Positive 2017 amount only came as a result of City borrowing money to pay bills. Values above do not include the missed annual payments to the pension funds.

# City General Fund Balance 2012-2019

The City's 2019 audit resulted in a general fund balance of negative \$27,748,362 in 2019. This does not include the value of the missed annual payments to the pension funds (Approximately \$39.8m as of 12/31/21, meaning the amount is even higher now due to interest).

Audited City General Fund Balance Year Ending 2012-2019



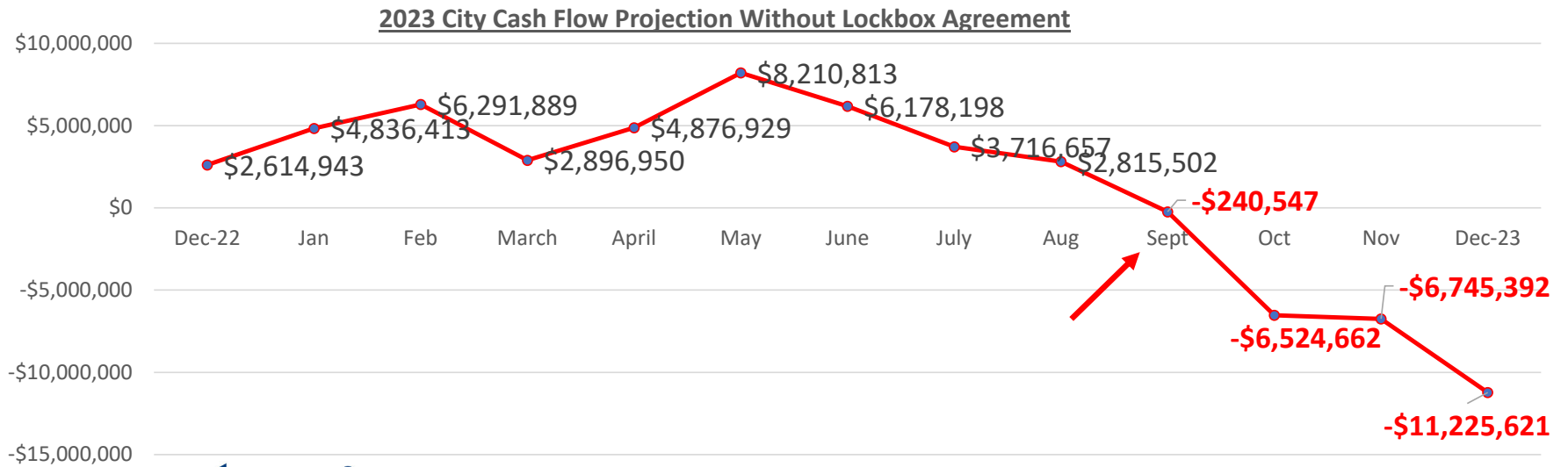


# Current City Cash Flow Projection for 2023

- The City will shut down without cash, so the Receiver’s team projects the City’s cash flow based on data received from the City’s finance department.
  - This report is called the “Cash Flow Report.”
- Earlier this year, the City was on track to run out of money in September due to the City’s structural deficit and a dispute with its bondholders over Covanta and Harrah’s revenues.
- Thanks to an agreement with the bondholders negotiated by the City’s bankruptcy conflict counsel Hangley Aronchick (“Lockbox Agreement”), we do not currently project the City running out of money this year. However, the projected year-end result is still extremely concerning and could change for the worse if the City’s expenditures come in higher than expected as has happened in the past.

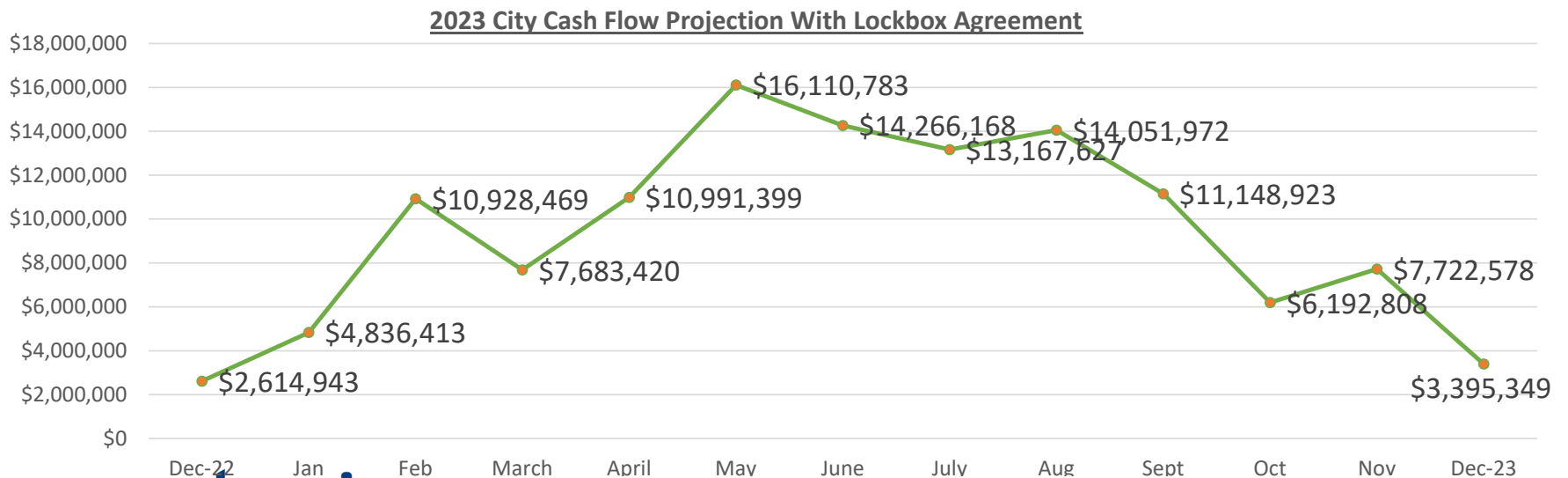
# 2023 City Cash Flow Projection Without Lockbox Agreement

Without the Lockbox Agreement, we projected that the City would have run out of cash in September of this year.

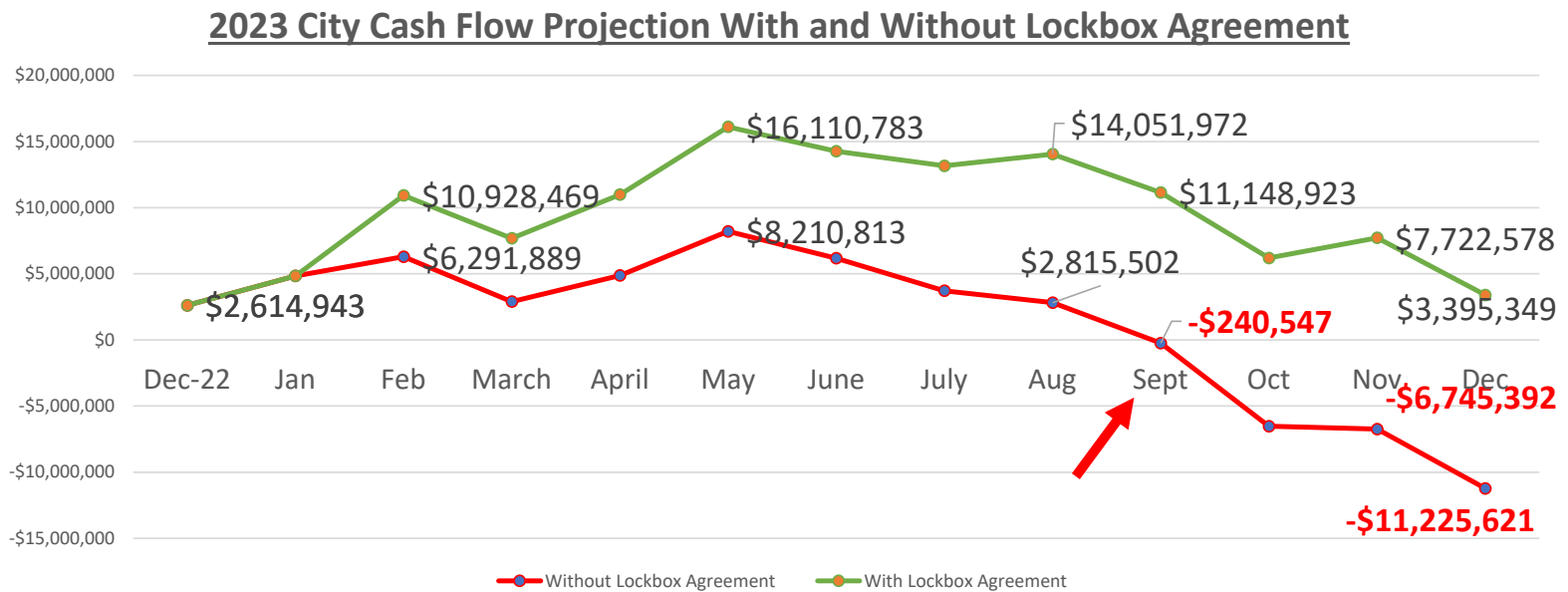


# 2023 City Cash Flow Projection With Lockbox Agreement

With the Lockbox Agreement, we project that the City will end the year with approximately \$3.4 million in its general fund. However, that is an extremely low amount for a city like Chester.



# 2023 City Cash Flow Projection With and Without Lockbox Agreement



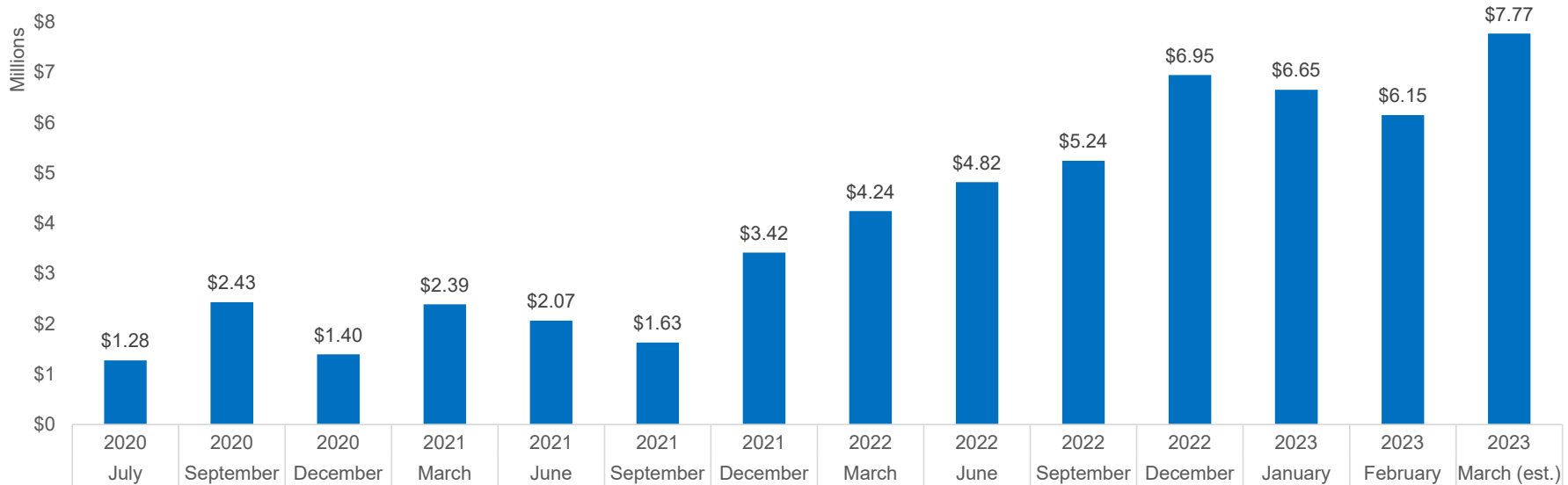
# 2023 City Cash Flow Projection

- Although the projection shows a positive \$3.4 million in the general fund at year end, the amount that the City actually is able to spend is closer to \$2.4 million due to outstanding checks to vendors that have not been cashed and EIT revenues that need to be deposited into the pension funds
- \$2.4 million is only about 16 days of operations
  - Per Government Finance Officers' Association best practices, the general fund balance should be at least \$9.5 million.
  - Additionally, this amount does not include money for additional necessary services such as animal control.
- The City will still need the \$5 million interest free tax anticipation loan from the Commonwealth in order to make payroll in January 2024.

# Police Pension Fund Since Receivership

Since the Receiver was appointed, we have been able to improve the amount of funds available to pay police pension benefits from approximately \$1.28 million in July 2020 to approximately \$7.77 million in March 2023. However, the fund is still severely underfunded.

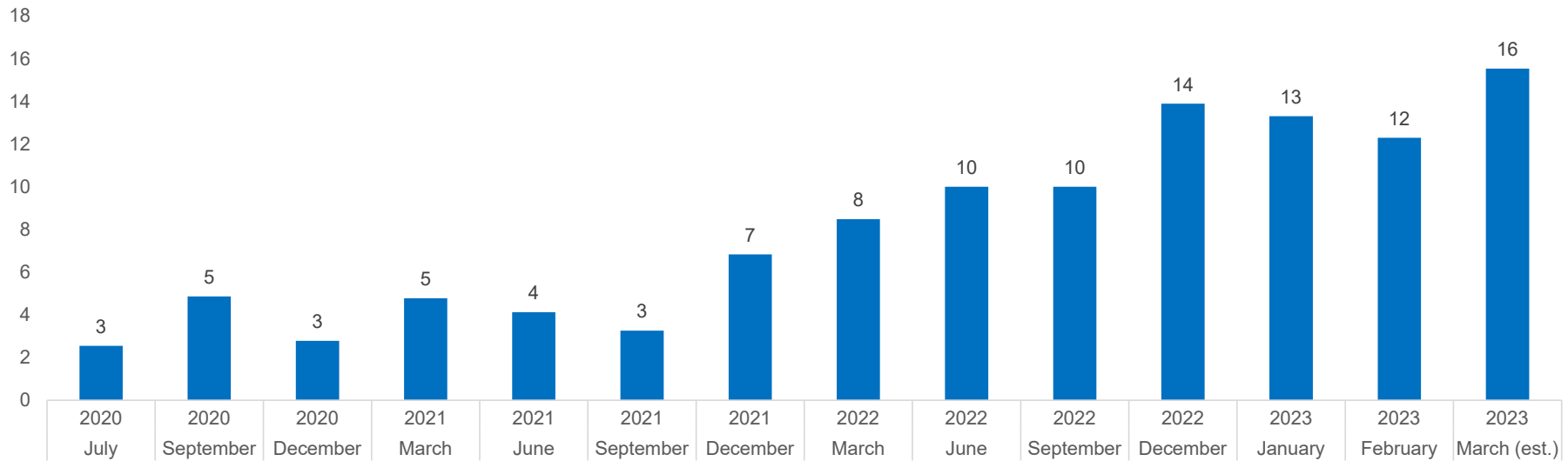
Police Pension Fund Cash Available for Monthly Benefit Payments



# Police Pension Fund Since Receivership

Since the Receiver was appointed, we have been able to improve the number of months the police pension fund can pay pensions from 3 months in July 2020 to 16 months in March 2023. The fund is still severely underfunded.

Police Pension Fund Estimated Months for Remaining Benefit Payments



# 5-Year Projection

- Although the next set of five-year projections has not yet been finalized, the City is still on pace to face an operating deficit in 2024 and an insurmountable deficit in 2025 absent an implemented solution.
- At the September 13, 2022, MFRAC we showed the City facing a \$12.4 million budget deficit in 2025 due to ARPA funds and another federal grant (SAFER) expiring.
  - The expiring ARPA funds alone will result in the layoffs of 12 people, including 5 in the public works department
  - The SAFER grant funds 8 firefighters whose jobs will also be at risk when that grant runs out



# Status of Bankruptcy & Plan Modification Litigation

# Status of Litigation

## *Overview*

- Certain City elected officials have appealed both the bankruptcy opinion finding Chester eligible for Chapter 9 bankruptcy and the Commonwealth Court order confirming the plan modification which included confirming the Receiver's power to suspend the administrative duties of elected officials to serve as day-to-day department heads.
  - Because of the Commonwealth Court appeal, City Council members are back as department heads while the Pennsylvania Supreme Court hears the case.
- These appeals have and will continue to delay the Receiver's efforts to address the City's critical financial and operational problems. Despite being in a fiscal emergency for three years, these elected officials have not put forth any credible alternative plan to solve the City's problems.

# Status of Bankruptcy Matter

- Mediation began on January 13, 2023
- On March 14, 2023, Judge Ashely Chan ruled that Chester was eligible for chapter 9 bankruptcy concluding:
  - “[T]he City has been and remains insolvent despite the Receiver’s ... extensive prepetition efforts to cut expenses and find sources of funding...[G]iven that the City’s residents are burdened by high taxes while essential services are diminishing, the City’s residents will be prejudiced should this Court deny Chapter 9 relief. Indeed, the City’s goal in this Chapter 9 case is to confirm a plan that ‘provides [a] permanent solution for the City of Chester and its residents.’ Accordingly, the Court finds the City filed this [bankruptcy] petition in good faith.” Opinion at p. 41

# Status of Bankruptcy

## *Certain Elected Officials' Appeal of Bankruptcy Decision*

- On March 28, 2023, the majority of elected officials filed a notice that they would be appealing Judge Chan's decision.
  - Note: the bondholders who also initially objected to eligibility have not filed an appeal.
- Litigating this appeal is going to cost time and money that the City does not have and makes little sense given the City's undisputed financial problems.
  - Recall earlier slide showing a general fund balance of negative \$27.7 million in 2019 and \$39.8 million in missed pension payments/interest to the pension funds as of 12/31/21
- The Receiver will continue with the mediation process although the same attorneys who are assisting with the mediation will have to now also spend time litigating the appeal.

# Status of Plan Modification Litigation

- On January 31, 2023, Commonwealth Court Judge Ellen Ceisler issued an initial ruling approving parts of the Receiver’s plan modification including a provision that the Receiver could suspend the administrative duties of elected officials to serve as day-to-day department heads and appoint experienced professionals in their place.
- Judge Ceisler wrote:
  - “[T]he Court concludes that Receiver has the authority to remove City Council members from their assigned positions as department heads and to appoint experienced professionals in their place. **Based on the credible evidence presented at the hearing, the Court believes that such administrative changes are not only permissible, but necessary.**” Order at p. 28 (emphasis added).

# Status of Plan Modification Litigation

## *Excerpt from Judge Ceisler's January 31, 2023 Order*

- “The credible evidence presented at the hearing demonstrates that the City’s elected officials are not empowering Receiver in the eyes of the City’s employees. Rather, the evidence shows that City officials frequently ignore Receiver’s advice and directives, and even direct other employees in their departments to ignore his directives. City officials also have historically overlooked issues such as the unauthorized payroll payments to an incarcerated employee, the former police chief allowing his friends to boost their pensions by working extra overtime before retirement, and the City seven-year default on its MMO payments.
- These incidents, together with the evidence of widespread nepotism within the City’s government, demonstrate a pattern of City officials taking care of their own and intentionally turning their backs on wrongdoing within their departments. Further exacerbating these problems is the Mayor’s assignment of Council members as department heads based on their loyalty to City Council and Mayor’s own inclination in a particular year, rather than on the person’s actual qualifications to oversee a particular area. These practices cannot continue.”  
Order at p. 39.

# Status of Plan Modification Litigation

## *Elected Officials' Appeal of Judge Ceisler's Order*

- On February 7, 2023, a majority of the elected officials appealed parts of Judge Ceisler's ruling including the provision that suspended administrative duties of elected officials to serve as day-to-day department heads.
- On March 29, 2023, the Pennsylvania Supreme Court issued an order that it would be taking the case. The effect of that order is that it "stayed" (paused) the appealed parts of Judge Ceisler's decision including the provision that suspended administrative duties of elected officials to serve as day-to-day department heads. Therefore, until the Court issues a decision, elected officials are now again serving in the role of department heads.

# Status of Plan Modification Litigation

## *Supreme Court Case Timeline*

- The PA Supreme Court has issued the following expedited schedule to address the appeal of Judge Ceisler's decision:
  - City elected officials' brief due on April 13<sup>th</sup>
  - Receiver reply brief due on April 27<sup>th</sup>
  - City elected officials' reply brief due on May 4<sup>th</sup>
  - Oral argument in Harrisburg on May 24<sup>th</sup>
- There is no deadline as to when the Court would issue an opinion.



# Importance of Supreme Court Case

- The plan modification case before the Pennsylvania Supreme Court is critical to Chester's future and its importance cannot be understated.
- The Receiver (and the Commonwealth Court) firmly believe that the City needs experienced professionals, not elected officials, running the City's day-to-day operations, especially in light of its financial condition and the clear evidence presented during the confirmation hearing.
- Even if we are able to solve the City's financial problems through bankruptcy, if its operations are not also addressed through receivership, the City's residents will not receive the level of services they deserve.

# Where We Are Now

- Certain elected officials have appealed both the bankruptcy eligibility opinion and the plan modification order. The Court decisions in both of these matters will take months to resolve, which is time the City does not have.
- Without the Lockbox Agreement, the City would have run out of money in September. Even with it, the projected year-end general fund balance is critically low.
- In 2025, the City can no longer use ARPA funds and will incur an insurmountable budget deficit absent a comprehensive solution.
- A comprehensive solution will likely take a year to implement meaning that the solution will need to be developed by the end of this year.
- The Receiver has been transparent about the City's financial condition and has tried to use the tools provided to him by Act 47.
- If a comprehensive solution is not found by the end of the year, there may be no alternative for Chester but disincorporation. The Receiver is trying to avoid that situation.

# Disincorporation

# Disincorporation

- Section 706(a)(12) of Act 47 gives the Receiver the power to recommend that the municipality be “disincorporated”
- Disincorporation means that Chester is “nonviable” and effectively would no longer exist
- Practically, this would mean that all City employees would be laid off, elected officials would be removed, and an “Administrator” would be appointed by DCED to contract for the provision of vital and necessary services on behalf of the area

# Disincorporation

## *“Nonviable” Municipalities*

- Criteria for determining whether a municipality is “nonviable” per section 431.1(a) of Act 47 (all criteria must be met):
  - (1) The municipality is unable to function as a general purpose unit of government to provide essential services to its residents and property owners.
  - (2) The municipality has experienced such deteriorated economic conditions and a collapse of its tax base that all reasonable efforts to restore economic viability have failed.
  - (3) Efforts to merge or consolidate the municipality with a neighboring municipality are unachievable or will not result in viability.

# Disincorporation

## *Section 439(a) of Act 47*

- Effects of disincorporation: On the date of disincorporation, the following shall occur:
  - (1) [T]he terms of office of all elected officials of the municipality shall end and no person shall be elected or appointed to fill any vacancy of office.
  - (2) All ordinances of the municipality shall be nullified.
  - (3) All corporate powers granted to the municipality under its charter, municipal code or any other provision of law shall terminate.
  - (4) The municipality shall be deemed by operation of law to be disincorporated. The area formerly contained within the municipality shall be an unincorporated services district...

# Conclusion

- The Receiver is trying to avoid disincorporation. However, just as the Receiver warned months ago regarding the possibility of bankruptcy, we need to do the same with disincorporation.
- Chester's financial situation is critical and the City is running out of time to find a solution.
- The City elected officials' appeals of the bankruptcy opinion and the plan modification order without any meaningful alternative plan are consuming valuable time and resources needed to focus on solutions.

End