

# Receiver Bankruptcy Update and Approach

MFRAC Meeting  
August 22, 2023

# Purpose of Presentation

- This presentation will:
  1. Update the public on the status of the bankruptcy process;
  2. Provide a high-level understanding of the Receiver's approach to the bankruptcy process including:
    - A. How the Receiver defines "Success"
    - B. Development of "The Number"

# Presentation Outline

- Bankruptcy Process Update
  - Background
  - Litigation
  - Mediation
- Receiver Bankruptcy Approach
  - Defining Success
  - Development of “The Number”

# Bankruptcy Process Update

# Bankruptcy Process

- Chapter 9 bankruptcies have three main phases (we are currently in the Mediation phase, although certain elected officials have appealed the eligibility determination):
  1. Eligibility Determination
  2. Mediation
  3. Plan of Adjustment
- Bankruptcy can be a long process
  - San Bernadino, CA took 10 years and 1 month
  - Puerto Rico took 4 years and 9 months
  - We are currently 9 months into this bankruptcy (Filed on November 10, 2022)

# Bankruptcy Background

- Receiver filed for bankruptcy on the City's behalf on November 10, 2022
- At the time of the bankruptcy filing, the Receiver asked for judicial mediation which was granted and is ongoing
- Despite Receiver's ability to reject contracts – including collective bargaining agreements – he has not done so
- City has continued to operate in normal course of business and is paying employees and vendors as it had prior to the bankruptcy filing.

# Bankruptcy Process Update

- There are currently three major litigation matters stemming from the bankruptcy that we will update you on. These cases involve:
  1. Determining the status of certain City debt
  2. Appeal by certain City elected officials of Bankruptcy Court's finding that City was eligible for chapter 9 bankruptcy
  3. Appeal by Aqua Pennsylvania of the Bankruptcy Court's decision finding that bankruptcy stay applies to the Pennsylvania Public Utility Commission (PUC) matter involving the potential sale of DELCORA to Aqua

# Bankruptcy Update - Litigation

## *Determining Status of Certain City Debt*

- In 2017 (prior to Receivership), Preston Hollow Advisors loaned the City \$19.2m to be used to refund debt and acquire a leased property
- Preston Hollow argues that this debt is “secured” by revenues the City receives from Harrah’s Casino and the Covanta Incinerator, meaning that they should get those revenues before the City does. The Receiver believes that the debt is not secured or “unsecured.”
- Under bankruptcy law, whether debt is “secured” or “unsecured” is very important because “secured” debt receives much more protection in bankruptcy
  - If the debt is found to be “secured” and the City needs to pay it, that will require the City to find additional revenues or cuts elsewhere



# Bankruptcy Update - Litigation

## *Determining Status of Certain City Debt (contd.)*

- The matter of whether the debt is secured or unsecured is being litigated in the Bankruptcy Court
  - The Receiver wants to have this issue resolved not only to help inform the Plan of Adjustment, but also for the City's 2024 budget
- On Monday, August 14<sup>th</sup>, the parties filed summary judgment briefs with the Bankruptcy Court
  - “Summary judgment” means that there is no significant dispute as to any material fact. Rather, the matter is really a legal question.

# Bankruptcy Update - Litigation

## *Determining Status of Certain City Debt (contd.)*

- The expected next steps for this litigation are:
  - A pre-trial conference set for September 18, 2023, before the Bankruptcy Court
  - The parties have agreed to ask the Court for any trial to occur (if the Court finds the need to resolve any factual disputes) by October 15, 2023
- Filings in this matter can be found here:
  - <https://www.donlinrecano.com/Clients/ccp/AdversaryProceedings>

# Bankruptcy Update - Litigation

## *Eligibility Appeal of Certain City Elected Officials*

- One of the threshold decisions that a bankruptcy judge needs to find is whether the municipality filing for bankruptcy was eligible for chapter 9 bankruptcy
- Only two entities challenged eligibility in bankruptcy court – bondholders and certain City elected officials
- On March 14, 2023, the Bankruptcy Court found that the City met the eligibility requirements
- Only certain elected officials appealed the Bankruptcy Court's decision

# Bankruptcy Update - Litigation

## *Eligibility Appeal of Certain City Elected Officials (contd.)*

- The appeal is pending in the U.S. District Court of the Eastern District of Pennsylvania before The Honorable Mia Roberts Perez
- The timeline of the appeal is as follows:
  - Certain Elected Officials filed a notice of appeal on March 28, 2023.
  - Certain Elected Officials, after seeking an extension of this deadline, filed their appellate brief on June 9, 2023.
  - The City filed its appellate brief on July 10, 2023.
  - Certain Elected Officials filed their reply brief on July 24, 2023.
  - *Status: We are waiting to hear from the Court. The Court could schedule oral argument or could proceed without oral argument.*

# Bankruptcy Update - Litigation

## *Aqua Appeal of Bankruptcy Stay of PUC DELCORA Matter*

- On May 23, 2023, the Bankruptcy Court found that the bankruptcy law litigation stay (“pause”) provision applied to the matter before the Pennsylvania Public Utility Commission (“PUC”) of Aqua Pennsylvania’s attempt to acquire DELCORA
  - Aqua Pennsylvania is a private water and wastewater company
  - DELCORA is the public regional wastewater treatment authority that serves much of Delaware County and which has its primary treatment facility on the Chester waterfront next to the Covanta incinerator
- The City’s interest involves assets that, per a 1973 agreement, revert back to the City in the event that DELCORA ceases to operate the system

# Bankruptcy Update - Litigation

## *Aqua Appeal of Bankruptcy Stay of PUC DELCORA Matter (contd.)*

- Aqua has appealed the Bankruptcy Court's stay because it wants the PUC matter to move forward
- Aqua's appeal is pending in the U.S. District Court of the Eastern District of Pennsylvania before The Honorable Mia Roberts Perez
- The timeline of the case is as follows:
  - Aqua filed a notice of appeal on June 6, 2023.
  - Aqua filed their appellate brief on August 7, 2023
    - Aqua's brief was due on August 4, 2023, but on August 2<sup>nd</sup>, Aqua filed a motion seeking a two-week extension of this deadline, which the City consented to.
    - On August 17, 2023, the Court entered an order deeming Aqua's brief timely filed
  - The City's appellate brief is due on September 6, 2023
  - Aqua's reply brief will be due on September 20, 2023

# Bankruptcy Update - Mediation

- At the time the Receiver filed for bankruptcy on behalf of the City, the Receiver asked for a judicial mediator to be appointed to lead confidential mediations between the City and creditors
  - Judge Mary Walrath, a Delaware bankruptcy judge, was appointed as the lead mediator by the bankruptcy court
  - Judge Walrath appointed Judge Steven Goldblatt, another Delaware bankruptcy judge, to mediate matters involving bondholders
- Under bankruptcy law, those mediations are confidential meaning that the parties cannot reveal what is being discussed.
- Mediations are on-going, however all parties are awaiting one piece of critical information – “The Number” that we will discuss later.

# Receiver Bankruptcy Approach Defining “Success”



# Defining “Success”

- Per Act 47, the Receiver is tasked with ensuring that residents receive vital and necessary services
  - Years of personnel cuts and inefficient operations have resulted in Chester residents not receiving adequate service levels.
  - To that end, it is not enough to just balance the budget. Chester needs to invest in its workforce and its infrastructure to provide adequate services.
- The Receiver defines success as ensuring that Chester can **financially and operationally** provide an **adequate level of vital and necessary services** on an **ongoing basis** in a **manner that is in the best interests of its residents**.

# Defining “Success”

- Key components of the Receiver’s view of “success” are:
  - Financial and Operational
  - Adequate level of vital and necessary services
  - Ongoing basis
  - Manner that is in the best interests of residents
- The next set of slides will further explain each of these components

# Defining “Success”

## *Financial and Operational*

- Receivership and Chapter 9 is not just about balancing budgets. It is also about ensuring that the City provides services to its residents, which after all, is the purpose of a city.
  - Balancing the City’s budget without taking into account the quality of service delivery to residents (discussed next) makes little sense.
- Improving City operations is also why the Receiver filed the Plan Modification on November 8, 2022.
  - We continue to await the PA Supreme Court decision on certain Plan Modification provisions appealed by certain elected officials. Oral argument on that matter was heard by the PA Supreme Court on May 24, 2023.

# Defining “Success”

## Adequate Level of Vital and Necessary Services

- It is not enough to simply say that the City is providing vital and necessary services. These services must be provided at an adequate level.
- Ensuring an adequate level of vital and necessary services will require additional personnel, increased compensation to recruit and retain certain employees and investment in City infrastructure.
  - It will also require improved efficiency and management.

# Defining “Success”

## Adequate Level of Vital and Necessary Services

- The concept of ensuring that a city can provide an adequate level of service is recognized in chapter 9 bankruptcy. The inability to do so is referred to as “service delivery insolvency.”
- In approving Detroit’s plan of adjustment, Judge Steven Rhodes found:
  - “A large number of people in [Detroit] are suffering hardship because of what we have antiseptically called service delivery insolvency... Detroit’s inability to provide adequate municipal services runs deep and has for years. It is inhumane and intolerable, and must be fixed.” (Oral Opinion on Record at p. 35)

# Defining “Success”

## Adequate Level of Vital and Necessary Services

- The question has been asked as to why the Receiver is adding positions requested by the City’s Chief of Staff when the Receiver warned about the possibility of disincorporation.
  - During the discussions about disincorporation, the Receiver was clear that the City’s “fiscal cliff” will occur in 2025 when American Rescue Plan Act (ARPA) money which is being used to maintain operations will expire. That has not changed.
  - The Receiver and his team are actively working to avoid disincorporation and need to proceed as if we will be able to reach a resolution that avoids it.
  - City residents need improved vital and necessary services now.
    - Many of the new positions are in the Codes department which has a clear connection to public health and safety and whose services will be at least in part funded by new fees.

# Defining “Success”

## *On an Ongoing Basis*

- “Ongoing” means sustainable over future years, not one-time
  - Recurring revenues must be greater than or equal to recurring costs
- Assumptions used in financial and actuarial modeling must reflect our best good faith estimates for what will occur in the future
- Controls and oversight also need to be implemented so that any plan of adjustment is followed since full recovery for the City will likely take years
  - There is a tendency to fall back into bad habits once the immediacy of the crisis fades and people stop paying attention

# Defining “Success”

## *In a Manner that is in the Best Interests of Residents*

- Oftentimes, financially struggling communities accept any new revenues they can get, regardless of community impact, since their tax bases alone often cannot support basic operations.
  - Such projects usually come with the promises of jobs for residents and have some support within the communities. It is only later, after the project is built, that the community feels the full impact of the decision.
- The Receiver does not think that dependence on revenues from industries with negative impacts on resident health is in the best interests of City residents and seeks to make a good faith effort to develop a plan of adjustment that does not require financial dependence on those revenues.
- The Receiver also understands the reality that eliminating dependence on these revenues cannot be done immediately.



# Defining “Success”

## *In a Manner that is in the Best Interests of Residents*

- Won't trying to reduce or eliminate the dependence on these revenues make it more difficult to fund City operations?
  - In the short term, yes. However, if a plan of adjustment is developed that relies on these revenues, the City will effectively be financially dependent on these industries continuing to operate in Chester for decades to come and the City's waterfront (which is often touted as an economic development opportunity) will likely continue to be used in its current manner.
  - If there is serious desire to change the uses of Chester's waterfront so that different economic development uses can occur (not only at the waterfront but throughout the City), then the first step is to try to eliminate or reduce financial dependence on revenues from industries that negatively impact the public's health.

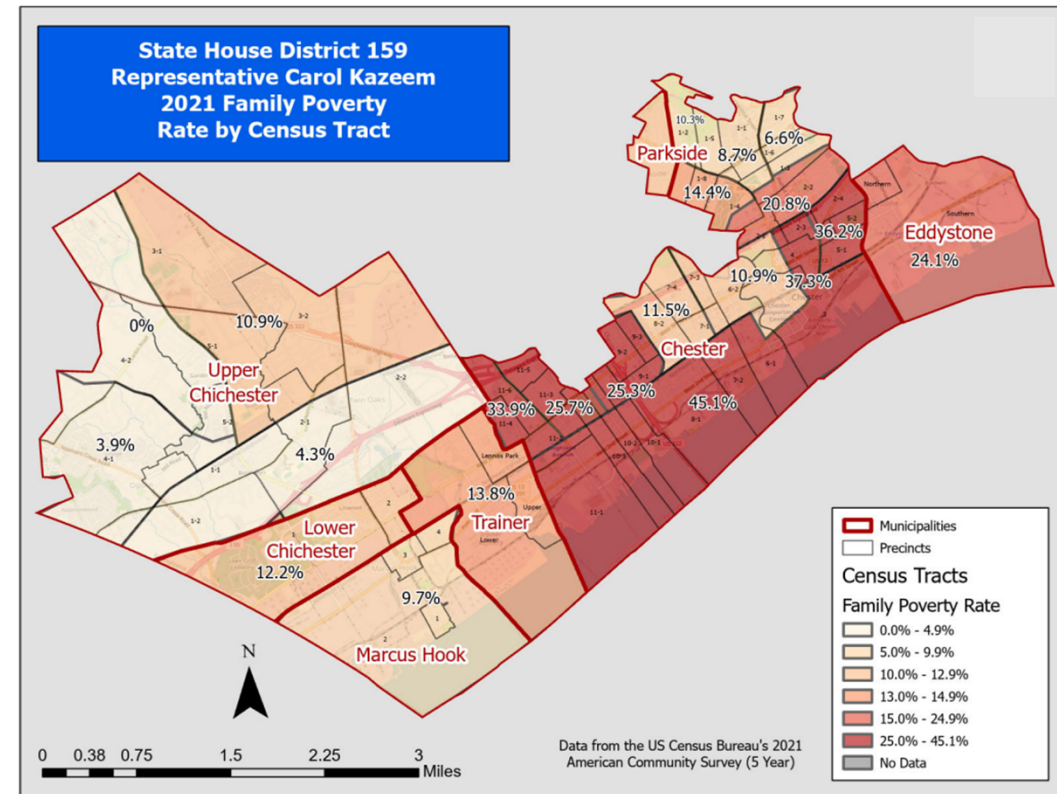
# Defining “Success”

## *In a Manner that is in the Best Interests of Residents*

- The following entities are located on Chester’s approximately 3.5 mile waterfront:
  - Harrah’s Casino: Provides \$10 million+/year to the City
  - State Correctional Institution - Chester: state jail
  - Kimberly Clark manufacturing plant
  - Subaru Park: Home of the Philadelphia Union
  - Covanta Incinerator: Provides approximately \$5 million/year to the City
  - DELCORA Main Wastewater Treatment Facility
- Note that several of these facilities provide significant benefits to people outside of Chester while Chester residents face all the negative consequences
  - To be clear, Chester residents also share some of the benefits of these entities; however, Chester residents experience all of the negative consequences.

*In a Manner that is in the Best Interests of Residents*

- Within that same 3.5 mile Chester waterfront, the family poverty rate is 45.1% which is significantly greater than other parts of Chester as well as other communities who are also bordered by the Delaware River.



# Defining “Success”

## *In a Manner that is in the Best Interests of Residents*

- The story of how the Covanta incinerator came to be built in Chester is particularly illustrative of the Receiver’s concerns. In chapter 5 of the book “Race and the Politics of Deception,” Professor Christopher Mele explains this history including that:
  - The desire to build a city-owned incinerator came from Chester City elected officials who saw it as “the cornerstone of the city’s plan for economic revitalization.”
  - “[The mayor] envisioned Chester as a ‘waste magnet’ profiting from packed landfills and looming trash crises in larger nearby cities such as Philadelphia and New York.”
  - “To build her case for the residents’ consent, the mayor reminded the audience of the importance of the incinerator as the best and last chance to address the city’s poverty, high crime rate, and declining tax base.”

# Defining “Success”

## *In a Manner that is in the Best Interests of Residents*

- “The mayor and other Chester officials launched an aggressive public relations campaign to build the incinerator. [The mayor] promoted the incinerator as the best opportunity for the city to secure its own economic development...The incinerator would generate between \$5 million to \$10 million a year from tipping fees and the sale of the electricity generated, three hundred new jobs with a minimum of 25 percent of the workforce minority employees, and up to one thousand additional jobs in new firms locating in Chester to buy and sell recyclable materials.”
- The City and Delaware County fought over which entity would build the incinerator, with Delaware County eventually winning out. The debate was not whether an incinerator would be built, but who would build it.

# Defining “Success”

*In a Manner that is in the Best Interests of Residents*

- City residents are still living with the impact of those decisions made 37 years ago including:
  - Financial dependency on revenues from the incinerator
    - Note that the City receives approximately \$5 million/year from the incinerator which was at the low end of the range cited in the book
  - Truck traffic to/from the incinerator
  - Location of the incinerator in Chester means that people are coming to Chester with garbage and some illegally dump it here which is a significant problem for the City’s public works department as well as being extremely disrespectful to Chester residents.

# Receiver Bankruptcy Approach Development of “The Number”

# Development of “The Number”

## *What is “The Number?”*

- The Receiver’s team has been in the process of trying to develop “The Number” which we define as the baseline expenditure level necessary for Chester to provide an adequate level of vital and necessary services.
- Developing “The Number” includes determining whether additional City personnel and services are needed (or not needed) as well as their respective compensation and costs. Additionally, this includes understanding and estimating the City’s true capital needs.



# Development of “The Number”

## *How Will “The Number” be Used?*

- Our approach is to start with “The Number” and then to identify the gap between the City’s revenues and what is necessary to fund “The Number.”
  - We believe that this is the correct approach as it does Chester’s residents little good to simply balance the budget (or not run of money) without providing adequate services (recall concept of service delivery insolvency from previous section)
  - We believe that this is the best way to ensure City Hall can provide vital and necessary services for the residents of Chester for years to come.

# Development of “The Number”

## *How Are You Developing “The Number”?*

- Developing “The Number” requires analysis of the City’s major operational expenditure areas which are:
  - Services that City employees provide
  - Services and supplies that third parties provide to City government and City residents
  - Capital expenditures (such as road repair, bridges, traffic signals and buildings)

# Development of “The Number”

## *Services that City Employees Provide*

- With the assistance of the City’s Chief of Staff and CFO, the Receiver’s team is meeting weekly to go department-by-department to analyze personnel needs and compensation
  - Previously, assessments have been completed for the fire department as well as the codes department. Assessments are ongoing for the police department, the public works department and the parks department
  - As part of this process, positions may be added or eliminated
  - We have completed approximately 1/3 of City departments thus far
- We expect to have this analysis completed by early October

# Development of “The Number”

## *Services and Supplies Provided by Third Parties*

- In addition to personnel costs, City expenditures also include supplies as well as services provided by third parties
- We are in the process of reviewing services third parties provide to the City as well as identifying services (such as animal control) that need to be provided
- With respect to supplies, one of the issues that we face is reliable, granular expenditure data. As discussed later, the City’s CFO is leading an effort to ensure accurate financial information

# Development of “The Number”

## *Capital Expenditures*

- The City of Chester has not had a recent, comprehensive assessment of its capital needs in several years
- The City is contracting with Herbert, Rowland & Grubic, Inc. (HRG) to conduct the following assessments:
  - Roadway assessments: City has 80 miles of City-owned roads
  - Bridge assessments: City has 9 bridges that it is responsible for
  - Traffic signal assessment: City owns 88 operational traffic signals
  - Building assessment
- HRG’s analysis will not only inform “The Number,” but it will also provide a framework for the prioritization and execution of capital projects going forward
- After a delay, City Council has approved contracting with HRG. We are currently awaiting contract execution for HRG to begin work.

# Development of “The Number”

## *What About Revenues?*

- In addition to developing “The Number” which is expenditure focused, we also need reliable revenue numbers which will be used to identify the gap between “The Number” and revenues
- The new Chief Financial Officer is leading an effort in the City’s Finance Department to ensure that we have accurate revenue and expenditure numbers
  - The Finance Department is nearly caught up with 2023 bank reconciliations which is important to understand City expenditures
  - We also continue to await the PA Supreme Court’s ruling in the Plan Modification matter which was heard by the Court on May 24, 2023

# Development of “The Number”

## *Why is this Taking So Long?*

- Chester does not have accurate and current financial data. The City’s new CFO is addressing this problem
  - In a typical Act 47 community, we use audited financial information or verified budget to actual information to place in the financial model. However, in Chester, the last audit is from 2019 and the City does not yet have a reliable budget-to-actual report. We have to build and verify the financials from scratch which is what the CFO (who began work on June 5, 2023) is doing.

# Development of “The Number”

## *Next Steps*

- Because the status quo situation hurts residents the most, and because the 2025 fiscal cliff is very real, the Receiver has every incentive to move as quickly as possible and is doing so.
  - By contrast, creditors benefit from things staying the same (until the 2025 fiscal cliff)
- The Receiver filed his Plan Modification on November 8, 2022, asking for relief to address these problems, but to date the matter is still in court. We are awaiting final resolution of that matter.
- Pending no additional unanticipated delays, we expect to have most of the “The Number” developed and more accurate financial data by mid-Fall of this year.



End