

# **EXHIBIT A**



535 Smithfield Street, Suite 700  
Pittsburgh, PA 15222

One Belmont Avenue, Suite 300  
Bala Cynwyd, PA 19004

John P. McLaughlin  
Attorney at Law  
Direct Dial: (610) 227-2596  
jmclaughlin@cdblaw.com

January 14, 2022

Lori Irwin, Esquire  
Chief Counsel  
Pennsylvania Department of Community and Economic Development  
Commonwealth Keystone Building  
400 North Street, 4<sup>th</sup> Floor  
Harrisburg, PA 17120-0225

In re: Receiver for the City of Chester's Requested Authorization to File for Bankruptcy  
on behalf of the City of Chester

Dear Ms. Irwin:

Your office has requested a summary of the justification for request by the Receiver for the City of Chester (the "City"), Michael Dowearly (the "Receiver"), for authorization pursuant to 53 P.S. Section 11701.706(a)(9) to file a municipal debt adjustment action under the United States Bankruptcy Code (the "Code"). The purpose of this letter is to provide that information.

The Receiver and his team previously discussed the rationale for the timing of this request with the Department of Community and Economic Development (DCED) and the Commonwealth, I think it is important to re-emphasize that rationale and how important the timing of this Request is to the Receiver's strategy going forward. Based on the facts, as outlined below, it is likely that the Receiver will need to act on and utilize the authorization to commence federal bankruptcy proceedings in the future; however, it is not his intent to commence such action immediately. Indeed, before commencing such a proceeding, the Receiver must and will engage in negotiations and discussions with City employees, unions, retirees and other creditors in order obtain concessions which would allow the City to avoid commencing Bankruptcy proceedings.

The negotiations with those groups will undoubtedly be very difficult. Some or all of the employees and retirees will likely resist engaging in any such negotitaions. The Receiver is requesting the authorization at this time in order to be able to be fully transparent with those groups so that they fully understand the consequences of any decision to not negotiate with the Receiver in good faith. The existence of the authorization, which would be revealed at the

535 Smithfield Street, Suite 700  
Pittsburgh, PA 15222  
412-395-1280

One Belmont Avenue, Suite 300  
Bala Cynwyd, PA 19004  
610-227-2591

www.cdblaw.com

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appropriate time during such negotiations, will provide a very high degree of transparency and credibility. It also will confirm that not only the Receiver views the City's financial situation as fiscally dire, but that the Commonwealth does as well.

As highlighted below, there is no doubt that the only way for the City to exit Receivership and secure its long-term financial future is to adjust its pension and post-retirement healthcare cost obligations. Practically, the only way of making the necessary adjustments absent agreement is through bankruptcy, but it is the Receiver's hope to avoid such a filing. The only way to do so is to credibly communicate that such a filing can and will occur if necessary and that the threat of losing benefits in a Bankruptcy proceeding is real.

The Receiver commits to informing and conferring with the Commonwealth once again before a bankruptcy proceeding is commenced. However, having the authorization during the negotiations discussed above is very important and will empower the Receiver during what will be very difficult negotiations. It is already known that the Receiver has also retained special bankruptcy counsel, Ballard Spahr LLP, to provide advice before any such filing and to handle the proceeding so this authorization will be just another step to show that the Receiver is serious.

#### Act 47 and Bankruptcy

The powers of the Receiver are outlined in Chapter 7 of Act 47. 53 P.S. Section 11701.701 et. seq. Section 11701.706(a)(9) of Act 47 outlines the Receiver's authority to commence a Bankruptcy proceeding and act on behalf of the municipality in that proceeding after receiving the written authorization of the DCED Secretary. 53 P.S. Section 11701.706(a)(9). That is the only limitation on the Receiver's power with respect to Bankruptcy under Chapter 7 of Act 47.

Although it is our view that only Section 11701.706(a)(9) of Act 47 controls a bankruptcy filing by the Receiver, Section 11701.261(a) provides guidance for authorization of applying for bankruptcy under the Code applicable to a municipality that has been declared to be in fiscal distress and operating under a Financial Coordinate under Act 47. That provision provides:

**(a) General authorization.** --A municipality is hereby authorized to apply to the department to file a municipal debt adjustment action pursuant to the Bankruptcy Code (11 U.S.C. § 101 et seq.), if at least one of the following conditions is present:

- (1) Imminent jeopardy of an action by a creditor, claimant or supplier of goods or services which is likely to substantially interrupt or restrict the continued ability of the municipality to provide health or safety services to its citizens.

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(2) One or more creditors of the municipality have rejected the proposed or adopted plan, and efforts to negotiate resolution of their claims have been unsuccessful for a ten-day period.

(3) A condition substantially affecting the municipality's financial distress is potentially solvable only by utilizing a remedy exclusively available to the municipality through the Federal Municipal Debt Readjustment Act (48 Stat. 798).

53 Pa. Stat. Ann. § 11701.261. Although the Receiver believes that this provision does not apply under Chapter 7 of Act 47, he believes the conditions are met as discussed further below.

Under Chapter 9 of the Code, only a "municipality" may file for relief. 11 U.S.C. § 109(c). There is no dispute that the City is a "municipality" under the Code. Section 109(c) of the Bankruptcy Codes sets forth four eligibility requirements for a municipality under Chapter 9:

1. The municipality must be specifically authorized to be a debtor by state law or by a governmental officer or organization empowered by State law to authorize the municipality to be a debtor;
2. The municipality must be insolvent, as defined in 11 U.S.C. § 101(32)(C);
3. The municipality must desire to effect a plan to adjust its debts; and
4. The municipality must either:
  - Obtain the agreement of creditors holding at least a majority in amount of the claims of each class that the debtor intends to impair under a plan in a case under chapter 9;
  - Negotiate in good faith with creditors and fail to obtain the agreement of creditors holding at least a majority in amount of the claims of each class that the debtor intends to impair under a plan;
  - Be unable to negotiate with creditors because such negotiation is impracticable; or
  - Reasonably believe that a creditor may attempt to obtain a preference.

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### Justification for Bankruptcy

The City has been under some form of Commonwealth oversight for the past 26 years. The City initially was declared to be fiscally distressed in 1995. Between 1995 and June 2002, the City operated under the oversight of a Coordinator under Act 47. On April 13, 2020, the Governor issued a Declaration of Fiscal Emergency in the City and the Receiver was appointed in June 2020. On December 28, 2021, the Commonwealth Court's extended the City's Receivership for another two years.

Since 2013, before the Receiver was appointed, the City avoided running out of operating cash by not paying its full legally mandated annual payments to its pension plans, otherwise known as its minimum municipal obligation (MMO). As a result, the police pension plan is approximately 3% funded which amounts to less than four months of benefit payments. The City's police pension fund had only \$2,567,027 in assets which is equivalent to approximately four to five months of pension payments. However, the \$2,567,027 in pension funds includes approximately \$1,149,000 set aside for officers participating in the City's Deferred Retirement Option Plan (DROP) program.

Due to its failure to make its previous MMO payments, the City has a debt or pension obligation of \$32,400,000 in MMO payments and interest payments to the police pension plan. The \$32,400,000 amount is a debt or pension obligation that the City owes and must pay to the pension fund under Act 205 and is over and above the annual Act 205 pension MMO contribution. The City also owes \$2,064,489 to its O&E pension plan and \$2,134,303 to the firefighter pension plan for previous skipped MMO payments plus interest. Therefore, for the City to be current on its pension obligations, it needs to pay that outstanding \$32,400,000, \$2,064,489, and \$2,134,303 in addition to the annual Act 205 pension MMO contribution. The City thus owes \$36,598,798 to its pension funds. The City has no assets or other viable means to make those payments. Even worse, the \$36,598,798 does not include the City's annual MMO payment to its pension funds which combined total more than \$11 million.

In addition to the foregoing MMO debt, the City has an unfunded pension liability for all of its pension plans. The City's unfunded pension liability totals \$67,173,192; however, that figure assumes that the \$36,598,798 that the City owes, but cannot pay, to all of its pension plans is in each pension fund. Thus, the unfunded pension liability is actually much higher. The City also has a post-retirement medical benefit obligation to its retirees that equals more than \$232 million, which is growing annually. The City has no savings or other money to fund this liability.

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The City's pension and OPEB liability ("Legacy Costs") are high because of the rich benefits that the City has provided over the years, especially to its police and fire bargaining units. The City acted in 2017 to curb the rich benefits for new hires, but the City still owes the benefits to its retirees and to the employees hired prior to 2017.

The City's residents also pay the second highest Earned Income Tax (EIT) in the Commonwealth even though they receive a low level of services. However, the City's staffing levels are so low outside of its police and fire services that the City cannot implement any more significant personnel cuts. To do so, the City would have to reduce the size of its police and fire staff, which is something the City cannot do due to operational needs.

In addition, the City would have had a negative cash flow in 2021 but was able to avoid that situation due to the use of one-time American Rescue Plan Act ("ARPA") funds. The City's operating result would have been even worse if the City had not re-directed more than half of its \$500,000 capital budget from its capital fund to its general fund to sustain operations during the year and help balance the budget. This transfer further delayed the City's ability to make critical improvements in its infrastructure. In 2022, the City's budget reflects a similar risk of insolvency. The City's 2022 budget is \$55.2 million, which will be covered mostly by General Fund revenue plus \$200,000 carried forward from 2021 and \$2.9 million from the American Rescue Plan Act of 2021 ("ARPA"). In order to prevent the City from running out of money before its real estate tax receipts came in, the Commonwealth of Pennsylvania provided the City with a zero-interest \$5 million emergency tax revenue anticipation note.

Based on the foregoing, the Receiver believes that the requirements for commencing bankruptcy proceedings are met under the Code. Although the Receiver does not believe that the requirements of 53 Pa. Stat. Ann. § 11701.261, quoted above, apply, those requirements are met or will be met as well, specifically the requirements of § 11701.261(a)(2) and (3). Based on the foregoing facts, the City will not be operationally or fiscally viable unless it reduces its pension and retiree health care costs.

The Receiver will engage retirees in discussions to do so, but it is very unlikely there will be any amicable resolution because the cuts to retiree benefits will have to be significant. Absent such an agreement, the only way to achieve such savings is through bankruptcy, which is why the Receiver is requesting this authorization pursuant to 53 P.S. Section 11701.706(a)(9). It is also essential, as outlined above, that the Receiver receive this written authority before he engages in negotiations with retirees. Although the City's debt to third parties, other than pension and OPEB debt, is not significant relatively speaking, the Receiver would use this authority to facilitate discussions with those parties as well.

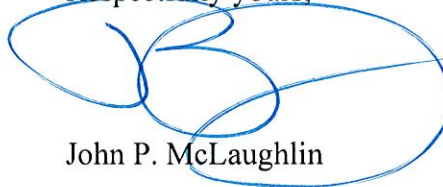
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Accordingly, 53 P.S. Section 11701.706(a)(9) of Act 47, the Receiver respectfully requests that the Secretary provide him with a written authorization to file a municipal debt adjustment action under the Code (11 U.S.C. 101 et seq.) and to act on the City's behalf in that proceeding. As a matter of convenience, the Receiver provides the following as a suggested specific written authorization:

Please be advised that pursuant to 53 P.S. Section 11701.706(a)(9) of the Pennsylvania Municipalities Financial Recovery Act ("Act 47"), the written unconditional authorization and consent of the Secretary of Community and Economic Development of the Commonwealth of Pennsylvania (the "Secretary") is hereby granted. All appropriate authority and powers are unconditionally conferred upon the Receiver for the City of Chester to institute, file, and pursue on behalf of the City of Chester the filing of a municipal debt adjustment action under the United States Bankruptcy Code, 11 U.S.C. Section 101 et. seq. (the "Code") to the fullest extent permitted under the Code and applicable law. As part of this written consent, the Secretary unconditionally and without limitation authorizes and consents to the Receiver for the City of Chester to act on the City of Chester's behalf and to take all other necessary and appropriate action during that proceeding and under the Bankruptcy Code in order to enable the City to adjust all debts and all financial obligations, including but not limited to pension and post-employment health and other benefits. The Receiver is authorized to take all action necessary to allow the Receiver, on behalf of the City, to take and receive the full benefits of such a filing and of the municipal debt adjustment action, without conditions or limitation.

Thank you for your consideration in this matter. Should you have any questions concerning this agreement, please do not hesitate to contact me. On behalf of the law firm, we truly appreciate the opportunity to represent the Office of the Receiver.

Respectfully yours,



John P. McLaughlin

cc: Sean Campbell, Esquire