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## MEMORANDUM FOR CITY COUNCIL MEMBERS

March 31, 2011

### Evaluation of Alternatives Available to the City of Harrisburg to Address Its Current Financial Situation

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**Evaluation of Alternatives Available to the City of  
Harrisburg to Address Its Current Financial Situation**<sup>1</sup>

I. EXECUTIVE SUMMARY

A. Background

Harrisburg's principal financial problems can be grouped roughly into two categories: structural deficits, that is, ongoing budget strains resulting principally from weakening tax and fee receipts coupled with mounting expenditures, and financial obligations arising from the City's guaranties of THA Facility-related obligations in the total current principal amount of approximately \$242 million. As a result of these two principal financial problems, among others, the DCED declared Harrisburg a distressed city under Act 47 on December 15, 2010.

The Facility-related debt comprises a combination of bonds that THA issued to the public, a swap agreement and a note that it issued to Covanta. THA's Facility-related bonds are revenue bonds, which are secured by and to be paid from the stream of income from the Facility. The City has guaranteed all THA Facility-related bonds. Assured has insured all THA Facility-related bonds, and the County has also guaranteed a significant portion of these bonds. If THA does not make a bond payment when due, the City, the County (if applicable) or Assured is required to make the payment. As between the City, the County and Assured, the City is primarily liable,

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<sup>1</sup> We have not independently verified the completeness or accuracy of any of the information provided to us, including documents. At least in some cases, we received inconsistent information. The analysis in this Memorandum is based upon the facts as we understand them at this time and as we have been able to determine to date. Nothing in this Memorandum shall be construed as an admission of any fact or legal position, and nothing shall preclude the City, including the City Council, based on additional factual information, legal analysis or otherwise, from taking a position in litigation, a chapter 9 case or otherwise that is inconsistent with any fact stated or position taken in this Memorandum.

and the County is secondarily liable, so that the City is liable under its guarantee to reimburse any payments that the County or Assured makes.

THA has not made all payments required on the bonds. The City has not made all payments it was required to make under its guaranties, that is, the payments that THA missed. Neither THA nor the City has replenished the debt service reserve funds for the bonds as required under the relevant indentures for the bonds. The County and Assured have made all payments on the bonds that THA and the City have missed to date, but have not made any payments to replenish debt service reserve funds.

Assured, the County, various indenture trustees for the bonds and Covanta have sued the City. Among other remedies, they seek a “writ of mandamus”, which is an order requiring the City and its Treasurer to apply all tax proceeds first to the repayment of the amounts the City owes under its Facility-related guaranties before being utilized for any other purpose, including the City’s operating expenses.

B. Act 47 and Chapter 9 Procedures

Neither Act 47 nor chapter 9 is a solution to Harrisburg’s financial distress nor an alternative to addressing its underlying problems. Each is only a process by which a solution may be reached. They are not mutually exclusive processes. Rather, they are integrated processes that work together if a chapter 9 filing becomes necessary. The goal is a solution to Harrisburg’s financial distress that will be embodied in a plan, whether adopted under Act 47 alone or also under chapter 9, that provides in detail how the City will address its structural deficits and financial obligations.

Act 47 and chapter 9 both contemplate a consensual plan, that is, one on which each of the major stakeholder groups agree. Achieving a consensual plan should be a paramount goal of either process, because of the savings in time, expense and



uncertainty that will result. However, an Act 47 plan can be implemented only if the plan is fully consensual, that is, if all stakeholders agree. By contrast, a chapter 9 plan can be approved by the court and made binding on dissenting creditors under certain circumstances, as described in more detail below.

Act 47 provides a city tools to use to create an Act 47 plan, such as the services of management and economic consultants who can advise on operational improvements and on the economic and financial effect of changes that the Act 47 plan may propose; the centralization of plan negotiations; higher priority access to certain Commonwealth funds; access to a Commonwealth loan fund to meet operating expenses on a temporary basis; and the ability to raise taxes, with a court's approval, above ordinarily applicable statutory limits. Chapter 9 provides protection from creditor collection actions; the ability to reject executory contracts; and the ability to bind dissenting creditors to a chapter 9 plan that discharges a portion or all of their claims as long as the court determines, among other things, that the city is doing all that can reasonably be expected under the circumstances to meet its obligations, whether that involves raising taxes or fees, cutting expenditures or selling or otherwise monetizing property.

Act 47 operates effectively only where all stakeholders agree on an Act 47 plan, but the only sanction resulting from a failure to agree falls on the city, not on any of the other stakeholders: the suspension of funding of all Commonwealth grants, loans and payments to the city (except for certain "pass-through" payments from the federal government). Act 47 does not expressly stop litigation or debt collection activities against the city nor bind stakeholders to a solution that affects them, such as a partial discharge of a claim or the resetting of a contract, to which they do not agree. Chapter 9

permits a city to gain court approval of a nonconsensual chapter 9 plan and “cram down” the chapter 9 plan on a dissenting class of creditors, but that approach is likely to involve significant litigation. Neither Act 47 nor a Harrisburg chapter 9 can affect THA’s obligations on its Facility-related bonds nor the County’s obligations on its guaranties. Nor, importantly, does chapter 9 operate simply to cleanse a city of its debt. Any discharge of debts comes only at an uncertain but likely significant cost.

If it is not consensual, a chapter 9 case can hurt a city’s reputation for business and in the credit markets, takes substantial time and attention away from the rebuilding and growth needed to restore the city’s health and subjects it to the risk that the court may dismiss the case, leaving the city unprotected and without any mechanism to implement a payment plan. A non-consensual chapter 9 case hurts creditors as well, by permitting the city to suspend payment of its obligations during the bankruptcy and by subjecting creditors to both the risk of losing—if the city proposes and the court approves a chapter 9 plan that substantially reduces the city’s obligations—and to the risk of winning—if the court does not approve the chapter 9 plan and dismisses the case, leaving the creditors with competing mandamus actions that could destroy the city and no clear avenue to recovery. And the delay, uncertainty and cost of litigation inherent in the bankruptcy process can hurt both the city and its creditors.

Act 47 and chapter 9 require the city council’s approval of an Act 47 plan and of a chapter 9 plan. Neither the Coordinator nor the bankruptcy court can impose solutions or a plan on the city. In addition, a chapter 9 court may not interfere with any of the city’s political or governmental powers, including its use of property or its payment of expenses. The court may not displace Commonwealth procedures, such as

Act 47, that apply to Harrisburg. The Act 47 process continues during a chapter 9 case, and the Coordinator remains a central player in developing the chapter 9 plan.

Therefore, the City should actively engage with its creditors and the Coordinator in serious negotiations to resolve its financial problems. If negotiations succeed, a chapter 9 filing likely becomes unnecessary. But the City should not rule out the possibility of a chapter 9 filing. That possibility and the power the filing can bring to bear on creditors may provide negotiating leverage that is not available where chapter 9 has been ruled out as an option, for whatever reason. The possibility of a filing and of the automatic stay of litigation may also deter disruptive or debilitating creditor collection action, such as continued pursuit of multiple mandamus proceedings that could starve the City of tax revenues, while negotiations are proceeding. There is another reason to engage in good faith negotiations with creditors for a complete resolution of the City's financial problems. Chapter 9 generally requires such negotiations as a precondition to filing for bankruptcy, although they may be excused where a city reasonably believes that a creditor is attempting, through judicial action, to obtain payment ahead of other creditors (as may be the case here).

The bondholders are protected by Assured's insurance and the County's guarantee (where applicable). Therefore, they are unlikely to engage in any sort of restructuring negotiations that would result in a reduction of the amounts owing to them on the bonds. Instead, Assured and the County, as well as Covanta, will be the parties principally at risk from the City's nonpayment of amounts owing under its guaranties.

### C. Evaluating Alternatives

The City's currently available cash resources are insufficient to meet its currently maturing obligations, especially those arising from the current and foreseeable shortfall of the Facility's revenues to service the Facility-related debt. A solution to the City's financial distress requires bridging the gap between available cash and maturing obligations. It appears that no affordable or foreseeable amount of tax or fee enhancements or expenditure reductions alone would be adequate to enable Harrisburg to meet its Facility-related debt obligations. Therefore, some combination of operational improvements, budget adjustments, revenue enhancements, expenditure reductions (including potentially from contract renegotiations), asset sales or other forms of asset monetizations, debt refinancings and debt reductions or other adjustments will likely be required to achieve a solution.

Making these elements come together to create a complete solution will require careful structuring. No single element appears to be adequate to bridge the entire gap. Nor is a piecemeal solution likely to succeed. A plan, whether under Act 47 alone or under chapter 9 as well, should lay out all of the transactions and changes that make up the plan and, to the extent possible, provide for a substantially simultaneous closing of any material transactions. The elements listed below should be evaluated as possible pieces of a complete solution, which must be lined up in the weeks or months following agreement on a plan and before final implementation. Elements of a solution might include:

- **Long-term lease or concession agreement of the parking system or sale of the parking lots and garages.** The HPA undertook an extensive bid process in 2007-08 and received a proposal from HPP for a 75-year lease

in exchange for a payment of \$215 million. HPP continues to express an interest in pursuing the deal. A payment of at least \$215 million could be used to retire or defease the HPA bonds and leave a substantial balance to the City (subject to compliance with Commonwealth law for transfer of funds from the HPA to the City) for a payment of the approximately \$65 million currently owing on the Facility-related obligations. Any remaining proceeds could be used to reduce amounts owing on the Facility-related debt as part of a complete refinancing of that debt. However, markets have changed dramatically since the tentative deal was struck with HPP in early 2008 and a new bidding process for some combination of lease, concession or sale might better test the current market. The HPA should note, however, that there is no assurance that HPP would participate or, if it did, that its offer would be on terms equal to or more favorable than those that are currently proposed. Nor is there any assurance that other bidders would be interested or would participate, as there do not appear to have been any other public expressions of interest since 2008.

- **Alternatively, improvements in parking system operations or increases in parking rates.** The parking system currently contributes revenue to the City's budget. HPP's proposal for a long term lease of the parking system suggests that revenue could be improved by the installation of electronic and other automatic collection equipment and by affordable rate increases. However, any such installation would require financing. Financing might be available from a concession agreement with a

commercial parking operator, who would operate the system for a fee, perhaps including a revenue sharing arrangement or from a refinancing of the HPA bonds. The City does not directly control the HPA, so any revenue enhancements from the parking system or other transaction involving the parking system would require agreement from the HPA board.

- **Sale of THA Facility.** The LCSWMA has delivered an unsolicited proposal to THA to acquire the Facility for \$45 million. The proposal affirmatively states that the LCWSMA would not assume any of the outstanding Facility-related debt of THA. The LCSWMA's proposal contemplates a dramatic reduction in tipping fees, but it has stated that it is open to a transaction involving alternative tipping fee rates for a higher purchase price.
- **Alternatively, operational improvements at the Facility; increases in tipping fees; and improved enforcement of flow control.** A study by R.W. Beck suggests renegotiation of the MPS with Covanta to provide greater certainty on certain matters and increased financial incentives to Covanta to improve operations and cash flow. The LCSWMA proposal also highlights possible operational improvements. Facility operational improvements could increase THA's ability to contribute to debt service payments on Facility-related debt, reducing the City's guarantee burden. We understand that City tipping fees of \$200/ton are substantially above market and that County tipping fees of about \$72/ton are also above market, although less so. This provides an economic incentive for haulers

to disregard flow control laws. THA is responsible for flow control enforcement and, we are advised, has been addressing enforcement issues more aggressively recently. Any increase in tipping fees risks making flow control enforcement even more challenging. In addition, THA is under a contract with the County that sets County tipping fees.<sup>2</sup> However, the County is materially at risk in the absence of a solution to the City's financial problems (because of its secondary guaranty of much of the Facility-related debt), so it should have an incentive to contribute to an overall solution through some increase in County tipping fees or otherwise, and could possibly offer greater assistance with the flow control enforcement issue.

- **Expense reductions through improved management of City functions and revenue increases through enhanced collection activity for taxes, fees and fines.** The Coordinator's Act 47 Plan is likely to address these matters as well as other tools to help the City operate more efficiently. However, the Coordinator's analysis is not yet complete, and these matters are beyond the scope of our engagement, so we do not comment on the contribution that these actions could make to bridging the gap.
- **Wage and benefit reductions based on renegotiation of collective bargaining agreements with the City's unions.** As with expense reductions generally, we are not in a position to comment on the value that might be available from a renegotiation of such contracts. The

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<sup>2</sup> Note that a past attempt to increase them was unsuccessful.

Coordinator may comment on appropriate modifications to such agreements. The unions and their members might be motivated to renegotiate based on their desire to restore the City's financial soundness and by the possibility of legal challenges to the extension of the current term of the contracts by the former Mayor and by the risk that the contracts may be rejected, and new terms and conditions of employment imposed, in a chapter 9 case. On the other hand, the City presumably would not welcome labor unrest at this delicate time.

- **Increases in various taxes or fees, including property taxes, earned income taxes on City residents, commuters or both, poured drink or other consumption taxes and parking taxes.** Tax rate increases, however, do not always result in higher revenues, because higher taxes can result in increased tax defaults, in lower property values and in flight from the City, lowering total receipts. Balancing tax rates and the population's ability to pay them requires careful economic analysis that is beyond the scope of our engagement but is likely within the scope of the Coordinator's assignment. We recommend careful review of any such analysis that is included in the Coordinator's report and Act 47 Plan.
- **Increase PILOT (payment in lieu of taxes) payments.** Over 45% of real property within the City is tax-exempt, including many Commonwealth buildings. The Commonwealth does make some contributions to the City's expenses and nonprofit organizations within the City make some payments. However, we do not have city-level data on PILOT payments to evaluate how they compare with the tax payments that would be made



if those entities were not tax-exempt. It may be worth evaluating whether PILOT negotiations with the Commonwealth or the imposition of some increased payment obligation for nonprofit organizations could provide additional budget relief.

- **Refinancing some or all of the bonds for which the City is liable, including GO bonds and the Facility-related debt, for a lower amount based on paydown from other sources and at a lower interest rate.** A refinancing based on a complete resolution of the City's financial problems might result in a lower overall interest rate, reducing debt service obligations. However, there are limitations on refunding municipal bonds and preserving tax-exempt status. These would have to be investigated carefully to ensure that the refinancing would provide the benefit of lower rates.
- **Seeking credit support or other contributions from Assured for any refinancing.** Assured will likely oppose any effort by the City to obtain a reduction in the amounts owing under the Facility-related debt unless the City has tapped all reasonable sources of value to bridge the gap. However, Assured may be willing to contribute to a solution in other ways, such as by contributing insurance on refinanced bonds or helping defray the underwriting or other costs of a refinancing transaction.
- **Sale of other City assets.** The A&M Assessment suggests that under current economic conditions, a City Island transaction would not generate any material amount of funds. Other City assets also would not likely provide material relief.

Some of these matters can be pursued by the City alone. Some require further information from the Coordinator. Some require cooperation from a City authority, such as THA or the HPA. Some require active negotiation with creditors. The City should be actively engaged with the Coordinator, who is ultimately responsible for formulating an Act 47 Plan, and with creditors and other stakeholders, to explore the values that each of these elements, among others, might contribute to an overall solution.

If the combined benefit of all the elements that are economically and financially feasible do not bridge the gap, then negotiations should proceed to the issue of debt reduction. A chapter 9 case could result in debt reduction in such circumstances. Generally speaking, a city is eligible to file a chapter 9 case only after it has attempted to obtain agreement from its creditors on a debt adjustment plan, and creditors will generally require that a city tap its available sources of value before agreeing to write off any amounts owing. The creditors with whom we have spoken have made it clear that that is their view in this case.

#### D. Negotiating Strategy Considerations

In selecting which alternatives to pursue and developing a negotiating strategy, the City Council should consider at least the following matters.

- If a writ of mandamus is issued in any of the pending litigation against Harrisburg and if its enforcement is not stayed by the Commonwealth courts, a chapter 9 case would be the only way to stay enforcement and prevent tax revenues from being diverted away from payment of the City's operating expenses. We do not view this as likely to occur if the City is actively engaged in good faith and meaningful negotiations with

its creditors. The City's creditors are sophisticated and fully understand that shutting down the City through the diversion of all tax revenue to payment of Facility-related obligations would likely destroy their ability to get paid anything close to the full amount they are owed. Moreover, it would be a pyrrhic victory for them if the City were immediately to file for chapter 9 after their attempt to enforce a mandamus order. If City services were terminated because the City were no longer able to pay for them, residents would gradually move out, property values and economic activity would drop, and tax collections would plummet. Even the tax collector could not be paid to collect the taxes. This would only exacerbate the challenges facing the City in repaying its creditors. However, if the City does not negotiate in good faith, the creditors will likely continue to aggressively pursue litigation as the only way to get the City to the negotiating table or to get any money at all, and the creditors will then argue that the City's failure to negotiate in good faith disqualifies the City from filing a chapter 9 case.

- As in most negotiations, the concessions that may be obtained will depend on the risk to the counterparty of not reaching an agreement and, more importantly, on the perception of that risk. Chapter 9 provides the threat that there will be a substantial delay before a creditor receives payment and that at the end of the case, the court may conclude that the City's proposal provides the creditor all that can reasonably be expected under the circumstances. Conversely, the City runs the risk that the court will find otherwise.

- Creditors may be willing to adjust their claims under certain circumstances. The two principal motivations are a borrower's inability to pay and the risk of a defect or flaw in the creditor's claim. The risk of litigation in a chapter 9 case over confirmation of a chapter 9 plan may also provide some motivation, but that depends on the City's and the creditor's evaluation of the strength of their respective litigation positions. In some cases, however, a creditor will disregard the litigation risk in an individual case if it has an institutional reason to resist compromising on a particular position, such as to protect its position in future negotiations with others. In some cases, that is, a party is willing to lose a particular battle rather than lose the war by agreeing to a compromise that will then be used against it in future negotiations with distressed counterparties. We believe that dynamic may be at work here. Conversely, creditors sometimes compromise to preserve a future business relationship. Thus, a creditor's willingness to compromise depends heavily on the particular facts, and there are no general numerical guidelines, least of all in municipal distress situations, because they occur so seldom. It is fair to say, however, that creditors do not typically compromise without a sound legal or financial reason to do so.
- A bankruptcy court will not approve a nonconsensual chapter 9 plan unless the City proposes to do all that can reasonably be expected under the circumstances. Those actions might include all of the elements listed above, to the extent that they are economically and financially feasible. Creditors are entitled to receive a reasonable recovery in a chapter 9 case,

and the municipality is entitled to retain sufficient tax receipts to provide the services that its residents require. Unless there is agreement with the major creditor constituencies on where the balance is, the City would be leaving the decision of whether the City achieved a reasonable balance in the court's hands, depriving the City of some control over its own fate.

- A city cannot be dismantled or liquidated, as a commercial corporation can, and chapter 9 does not permit the court to order either. Therefore, if the City is not able to reach agreement with its major creditor constituencies and the court does not approve the Chapter 9 Plan, the court's only sanction is to dismiss the case, leaving the City with a significantly impaired ability to fashion a comprehensive solution.

#### E. Conclusion

The City should be developing and actively pursuing a negotiating strategy. The Coordinator's draft Act 47 Plan is expected in about 60 days, and the City Council will have limited time to respond to the Act 47 Plan. An immediate move to chapter 9 is unlikely to address the City's financial problems successfully unless the City has first made a good faith attempt to negotiate a consensual agreement. Therefore, whatever role chapter 9 may have in the City's future, the Act 47 process and attempts to negotiate a consensual agreement with stakeholders must take center stage for now.

## II. INTRODUCTION

The Harrisburg City Council (the “City Council”) has engaged Cravath, Swaine & Moore LLP to advise the City Council on alternatives that may be available to the City of Harrisburg (the “City” or “Harrisburg”) to address its current financial situation, including an analysis of a proceeding under the Pennsylvania Municipalities Financial Recovery Act of 1987 (“Act 47”) and the filing of a case under chapter 9 of Title 11 of the United States Code (the “Bankruptcy Code”). On February 8, 2011, the City Council adopted a resolution to expand the scope of our engagement to include representation of the City Council as well as advice.

During the course of our engagement, we have met with many of the key stakeholders, including the Mayor and her staff, the former City Solicitor, the Executive Director of The Harrisburg Authority (“THA”) and its counsel and financial advisors, County Commissioner Haste and the County’s counsel and financial advisor, representatives of the Department of Community and Economic Development (the “DCED”), the Coordinator (as defined below), counsel to National Public Finance Guaranty Corporation, which has insured Parking Authority bonds, hotel bonds, and sewer and water bonds, representatives of Assured Guaranty Municipal Corporation (“Assured”), which has insured the Facility-related bonds, and representatives of Harrisburg Public Parking, LLC (“HPP”), a joint venture of Lambdastar Infrastructure Partners (“Lambdastar”) and EQT Infrastructure Limited.

We reviewed the documents underlying the City’s obligations on its bonds, notes and Guaranty Agreements, THA debt agreements, complaints relevant to our analysis that have been filed against the City in court, the City’s 2008 audited

financial statements and 2010 interim financial report, the General Overview of the Mayor's proposed 2011 budget, the October 20, 2010 DCED Consultative Evaluation under Act 47 (the "DCED Consultative Evaluation"), the January 2010 Management Partners report on an Emergency Financial Plan for the City, the Facility Appraisal (as defined below) and R.W. Beck Inc.'s ("R.W. Beck") Management Audit and Financial Analysis of the Harrisburg Authority's Resource Recovery Operations, dated February 23, 2011 (the "R.W. Beck Analysis"), among other things.

We researched the law on Act 47 and the operation of Act 47 on other Commonwealth cities and towns. We researched other Pennsylvania law that may have a bearing on the City's current situation, such as the Debt Act, the MAA, the LTEA, the Third Class City Code, the Optional Third Class City Charter Law and the PICA Act (in each case, as defined below). We researched issues under chapter 9 that might arise for Harrisburg.

Additionally, because legal advice must be predicated on a thorough and complete understanding of the facts and because the problems that face the City are as much financial problems as they are legal, we concluded that any advice on alternatives must include an analysis of their financial feasibility and impact. Accordingly, we retained the services of Alvarez & Marsal Public Sector Services, LLC ("A&M"), one of the premier financial advisory and turnaround management firms, who volunteered to provide its services to us on the same pro bono basis on which we are providing services and advice to the City Council. A&M provided a Restructuring Alternative Assessment to us (the "A&M Assessment") that provides certain analysis and data relevant to our findings and conclusions in this memorandum. A copy of the A&M Assessment is attached to this memorandum.

Our findings and conclusions from this review are set forth in this memorandum, which describes in detail the background, facts, issues and law, as well as the advantages and disadvantages of the City utilizing the Act 47 process alone or in combination with that of chapter 9 of the Bankruptcy Code.<sup>3</sup>

As noted in the DCED Consultative Evaluation, the City has experienced a pattern of (1) increasing year-end cash flow deficits; (2) an inability to pay current and future debt obligations; (3) declining tax revenue in constant dollars, taking inflation into account; (4) increasing annual costs, particularly in personnel and employee benefits; and (5) an unsustainable reliance on one-time revenue strategies. (p. 36).

On December 15, 2010, Austin Burke, the Secretary of the DCED (the "DCED Secretary"), made a determination that Harrisburg is financially "distressed" under Act 47, based on the City's having met the following criteria: (1) the City "has defaulted in payment of principal or interest on any of its bonds or notes or in payment of rentals due any authority" and (2) the City "has sought to negotiate resolution or adjustment of a claim in excess of 30% against a fund or budget and has failed to reach an agreement with creditors."<sup>4</sup> The first prong was met because the City failed to make payments on various debt obligations due and owing. The second prong was met because as of December 15, 2010, the City's unpaid debt obligations, unpaid vendor

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<sup>3</sup> We have not independently verified the completeness or accuracy of any of the information provided to us, including documents. At least in some cases, we received inconsistent information. The analysis in this Memorandum is based upon the facts as we understand them at this time and as we have been able to determine to date. Nothing in this Memorandum shall be construed as an admission of any fact or legal position, and nothing shall preclude the City, including the City Council, based on additional factual information, legal analysis or otherwise, from taking a position in litigation, a chapter 9 case or otherwise that is inconsistent with any fact stated or position taken in this Memorandum.

<sup>4</sup> 53 P.S. § 11701.201(3) and (9).



invoices and claims filed in the Dauphin Court of Common Pleas against the City equaled approximately 114% of the City's 2010 budget. On January 12, 2010, the DCED appointed The Novak Consulting Group ("Novak"), a management consulting firm based in Cincinnati, Ohio; Stevens & Lee ("S&L"), a law firm with a focus on governmental relations based in Reading, Pennsylvania; the Pennsylvania Economy League (the "PEL"), a non-partisan, nonprofit public policy and research organization; and O'Donnell Associates ("O'Donnell"), headed by Robert W. O'Donnell, as Harrisburg's Coordinator (as defined below).

### III. BACKGROUND

#### A. Introduction to the Parties

Harrisburg's current financial situation and its available options are complicated by the involvement of multiple parties, each with varying motivations and interests. It is important to understand each party's existing role, its potential role as part of an ultimate solution and what motivations will animate its actions.

The City is a third class city of the Commonwealth of Pennsylvania (the "Commonwealth"), operating in accordance with Third Class City Code, 53 Pa. C.S.A. § 35101 et seq. and the Optional Third Class City Charter Law, 53 Pa. C.S.A. § 41101 et seq. The City is organized under the Mayor-Council Plan A or "Strong Mayor/Council" form of government. The City was established as the capital of the Commonwealth in 1812. Mayor Linda Thompson took office in January 2010, replacing Mayor Stephen Reed, who had been the Mayor of Harrisburg for 28 years.

Harrisburg is located in the County of Dauphin (the "County"), which is a Third Class County of the Commonwealth. Harrisburg was established as the County Seat of Dauphin County in 1785.

The City Council has created a number of authorities to manage and provide services to Harrisburg's residents, including the Harrisburg Parking Authority (the "HPA"), the Harrisburg Redevelopment Authority (the "HRA") and THA. The City Council acted under the Municipality Authorities Act of 1945 of the Commonwealth of Pennsylvania, approved May 2, 1945, P.L. 382, as amended, 53 P.S. § 301 et seq. (the "MAA").

The HPA operates the City's parking system. It must deposit any parking revenues and any unrestricted administrative fund balance at least quarterly into a Coordinated Parking Fund as required under a "Cooperation Agreement for Downtown Coordinated Parking System" dated June 27, 1984, as amended and restated on March 16, 1994, between the City, the HRA, the Harristown Development Corporation, the Mayor, the City Council and the HPA. After making debt service payments on bonds secured by the Coordinated Parking Fund, any excess fund balance is transferred to the City annually. In 2007, the City received a refund of \$4,005,000, representing excess amounts deposited into the system for 2007. The City's excess parking revenue refund in 2008 was \$4,750,000.

THA provides water and sewer services to the citizens of Harrisburg and certain surrounding neighborhoods. In addition, THA owns a resource recovery facility (the "Facility"), which is a trash-to-energy incinerator that began commercial operation in 1972 and can process up to 800 tons of trash per day.

In 1993, THA purchased the incinerator from the City, but the City continued to operate it pursuant to a Solid Waste Management Agreement, dated as of December 1, 1993, between the City and THA. In 2003, Facility operations were discontinued, and THA retained Barlow Projects, Inc. ("Barlow") to undertake a major retrofit of the Facility to include three new furnace boiler combustion units, new air pollution control equipment, a new steam turbine generator and other associated systems and equipment. After significant delays and cost overruns, Barlow never successfully completed the project, and on December 31, 2006 THA terminated Barlow's involvement. On January 2, 2007, operations were turned over to Covanta Harrisburg, Inc. ("Covanta"), a Delaware corporation, which is the current operator of the Facility.

Harrisburg's guaranty of THA's Facility-related debt is one of the principal reasons for Harrisburg's current financial situation. The County is a secondary guarantor on much of that debt. Assured has underwritten the municipal bond insurer policies for THA Facility-related debt. Both THA and the City have been unable to meet their increasingly burdensome debt service obligations for the Facility debt, with the situation deteriorating to the point that the City's ability to make payments on its general obligation bonds<sup>5</sup> has been jeopardized.<sup>6</sup>

#### B. Selected Relevant History

In compliance with consent orders issued by the United States Environmental Protection Agency (the "EPA") and the Pennsylvania Department of Environmental Protection (the "DEP"), the City ceased the combustion of waste in the

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<sup>5</sup> General obligation bonds ("GO bonds") are unsecured municipal obligations that are backed by the full faith and credit of the issuer and are payable from general tax revenues.

<sup>6</sup> <http://www.nytimes.com/2010/09/03/business/03muni.html>

incinerator on June 18, 2003. The City and THA then determined to fund a project (the "Retrofit Project") to improve the Facility, which included a comprehensive retrofit/modernization of the Facility to bring it into compliance with federal and state air quality requirements and to upgrade the Facility so that it could effectively process waste into steam and electrical energy using state-of-the-art combustion technology. THA hired Barlow to complete the Retrofit Project. In late 2005, Barlow was substantially behind schedule and lacked sufficient cash, so it attempted to raise additional funding. Barlow obtained a \$25 million loan from CIT Capital USA, Inc. ("CIT"). In January 2006, THA entered into a series of agreements with CIT, which are currently the subject of litigation brought by THA against CIT. THA argues that the purported guaranty of Barlow's obligations to CIT in one of the documents was not authorized and is therefore unenforceable.<sup>7</sup>

Barlow was unable to complete the Retrofit Project,<sup>8</sup> and the City brought suit against Barlow on July 26, 2007 but, due to Barlow's insolvency, the City was able to recover only \$5 million, which Barlow paid to THA on November 23, 2009. This \$5 million was transferred into the 2003 D Construction Account, discussed below. The 2003 D Construction Account is controlled by the Retrofit Trustee (as defined below).

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<sup>7</sup> TD Bank, National Association, as trustee under the 2003 Indenture and Retrofit Indenture (each as defined below), and Manufacturers and Traders Trust Company, as trustee under the Trust Indenture dated as of August 15, 2002, filed an amicus brief in this case, arguing that if THA were forced to pay CIT \$25 million, then CIT would be improperly afforded a priority of payment superior to that of the bondholders under THA indentures.

<sup>8</sup> Barlow was required to achieve substantial completion of combustion unit 1 by March 14, 2006, combustion unit 2 by March 22, 2006 and combustion unit 3 by April 2, 2006. None of the three combustion units was substantially completed by its required dates and, as a result, the Facility was never able to meet the performance requirements of the contracts.

On January 2, 2007, operations of the Facility were turned over to Covanta, and Covanta currently operates the Facility. A Covanta affiliate was also engaged to complete the construction and equipping of improvements, including the comprehensive retrofit and modernization of the Facility (the “2007 Retrofit Completion Project”). The financing of the Retrofit Project and the 2007 Retrofit Completion Project is discussed in more detail below.

Since completion of the Retrofit Project, the net income generated by the Facility has not been sufficient to enable THA to make the scheduled debt service payments. The annual debt service due between 2010 and 2034 ranges between \$14,643,000 and \$27,569,410. (R.W. Beck Analysis, page 1).

#### C. Outstanding Debt

The following section summarizes debt obligations of the City most relevant to this analysis, including general obligation notes and bonds issued by the City and guaranties of certain debt issued by THA. Note, however, that this list is not comprehensive, as Harrisburg is also a guarantor of the debt of other governmental entities, including the HPA and the HRA, among others.

1. Harrisburg Direct General Obligation Debt

The following table presents the City's existing GO bonds:

<b>Harrisburg General Obligation Notes and Bonds</b>						
<b>Description</b>	<b>Series</b>	<b>Original Principal</b>	<b>Maturity</b>	<b>Insurer</b>	<b>Outstanding</b>	<b>Comments</b>
General Obligation Bonds	1997D	\$24,891,771	9/15/22	Ambac	\$17,415,619	Approved by City Council on 11/25/97 to fund capital projects and advance refund <sup>9</sup> Series B-1. Being repaid from General Fund real estate taxes.
General Obligation Notes	1997F	\$26,632,303	9/15/22	Ambac	\$20,817,338	Approved by City Council on 11/25/97 to fund capital projects and advance refund Series 1995 and Series A 1992. Being repaid from General Fund real estate taxes.
General Obligation Note	2003A	\$132,800	9/1/13	N/A	\$42,811	Approved by City Council on 06/10/03 for transportation infrastructure improvement projects. Being repaid from General Fund real estate taxes.
General Obligation Note	2003B	\$360,000	9/2/13	N/A	\$116,053	Approved by City Council on 06/10/03 for transportation infrastructure improvement projects. Being repaid from General Fund real estate taxes.
General Obligation Note	2003C	\$135,000	9/3/13	N/A	\$42,764	Approved by City Council on 06/10/03 for transportation infrastructure improvement projects. Being repaid from General Fund real estate taxes.

<sup>9</sup> See Section V(B)(4) – Refunding/Refinancing of Outstanding Debt.

<b>Harrisburg General Obligation Notes and Bonds</b>						
<b>Description</b>	<b>Series</b>	<b>Original Principal</b>	<b>Maturity</b>	<b>Insurer</b>	<b>Outstanding</b>	<b>Comments</b>
Guaranteed Revenue Notes	2006	\$7,200,000	5/15/16	N/A	\$5,310,000	Issued by the Harrisburg Redevelopment Authority. Proceeds and debt service responsibility held by the City. <sup>10</sup>
General Obligation Note	2008	\$2,400,000	3/15/18	N/A	\$1,994,317	State loan for resurfacing City streets. Being repaid from General Revenues of the City.
<b>Total</b>		<b>\$61,751,874</b>			<b>\$45,738,902</b>	

To date, the City has made all of its debt service payments on the existing general obligation debt. The following table provides a projection of the City's debt service requirements for the general obligation debt for fiscal year 2011:

<b>Harrisburg General Obligation Notes and Bonds – FY11 Debt Service</b>						
<b>Date</b>	<b>1997D</b>	<b>1997F</b>	<b>2003 AB&amp;C</b>	<b>2006 (estimate)</b>	<b>2008</b>	<b>TOTAL</b>
03/01/2011			\$2,028			\$2,028.77
03/15/2011	\$2,760,000	\$2,565,000				\$5,325,000
03/26/2011					\$297,742.41	\$297,742.41
05/15/2011				\$660,164		\$1,112,091.25
09/01/2011			\$67,903			\$67,903.98
09/15/2011	\$1,735,000	\$1,610,000				\$3,345,000
11/15/2011				\$90,773		\$292,175.50
<b>Total</b>	<b>\$4,495,000</b>	<b>\$4,175,000</b>	<b>\$69,932</b>	<b>\$750,937</b>	<b>\$297,742.41</b>	<b>\$10,441,941.90</b>

The following section summarizes the common features of the City's general obligation debt. Any variation from this general description is discussed in the applicable summary for that debt issuance.

(a) Common Features

The City's general obligation debt is supported by the full faith, credit and taxing power of the City for the payment of principal and interest on the bonds. In

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<sup>10</sup> This note was issued by the HRA, but the proceeds of the note issuance were given to the City, and the City is responsible for debt service on the note.

the authorizing ordinances for each of the bonds, the City covenanted that it would appropriate amounts from general revenues each year to cover the amount of debt service required for the bonds for the year and pay appropriate amounts into a sinking fund for each bond. Under the Local Government Unit Debt Act, 53 Pa. C.S.A. § 8001 et seq. (the “Debt Act”), holders of the GO bonds have a security interest in all amounts deposited in the respective sinking fund for that bond issuance.

The GO bonds bear interest, payable semi-annually or annually, at varying rates.

In accordance with the Debt Act, if the City defaults on payment of debt service for a period longer than 30 days, or fails to comply with provisions of the indenture governing a general obligation bond, holders of 25% of the aggregate principal amount of the applicable general obligation bond may appoint a trustee to represent them. Such holders may direct the trustee to take various actions on their behalf, including petitioning the Court of Common Pleas of Dauphin County to levy the amount due on the general obligation bond on all taxable property in the City in order to collect revenues for payment to the general obligation bond.<sup>11</sup> Once the trustee commences any action, individual holders of such general obligation bond are precluded from taking or continuing similar action.

Ambac Assurance Corporation (“Ambac”) issued a municipal bond insurance policy simultaneously with delivery of each general obligation bond to insure the payment of principal and interest on the GO bonds. Under the policy, Ambac is

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<sup>11</sup> § 8263(b)(5) of the Debt Act. Note that this remedy is different from that available under § 8261 of the Debt Act, which is explained further in Section II(F)(2).



obligated to pay to the United States Trust Company of New York any unpaid principal or interest that is due and unpaid by the City. Ambac will make such payments on the later of the date on which such principal and interest becomes due for payment or within one business day following the date on which it shall have received notice of non-payment from the applicable indenture trustee/paying agent. The insurance extends for the term of each general obligation bond and cannot be cancelled by Ambac. The insurance policy does not cover payment on acceleration or advancement of maturity, payment of any redemption, prepayment or acceleration premium or non-payment caused by the insolvency or negligence of the trustee or the paying agent. If Ambac makes a payment under the municipal bond insurance policy, Ambac obtains the bondholders' rights to payment from the City through subrogation. Thus, the City is not relieved of its payment obligation under the GO bonds when Ambac makes a payment to the bondholders. Rather, upon making such payment to the bondholders, Ambac is substituted in place of the bondholders with reference to a lawful claim, demand or right under the governing general obligation indenture, such that Ambac succeeds to the rights of the bondholders in relation to a debt or claim against the City and the bondholder's rights and remedies under the governing general obligation indenture.

In accordance with Rule 15c2-12 of the Securities and Exchange Commission (the "SEC"), the City must provide copies of its annual audited financial statements for each fiscal year<sup>12</sup> to the Nationally Recognized Municipal Securities Information Repository (the "NRMSIR") and the State Information Depository (the

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<sup>12</sup> Note that the most recently completed audit for the City was for 2008.

“SID”). Additionally, the City must provide notice to the NRMSIR and the SID of the following events if material:

- principal and interest payment delinquencies;
- non-payment related defaults under the ordinance;
- unscheduled draws on debt service reserves reflecting financial difficulties;
- unscheduled draws on credit enhancements reflecting financial difficulties;
- substitution of credit or liquidity providers, or their failure to perform;
- adverse tax opinions or events affecting the tax-exempt status of the GO 1997-D Bonds;
- modifications to the rights of holders of the GO bonds;
- calls of the GO bonds for redemption;
- defeasance of the GO bonds or any portion thereof;
- release, substitution, or sale of property securing repayment of the GO bonds; and
- rating changes.

(b) General Obligation Refunding Bonds Series D of 1997

On November 25, 1997, the City Council enacted an ordinance issuing General Obligation Refunding Bonds, Series D of 1997 (“GO 1997-D Bonds”) in the amount of \$24,891,771.10. The GO 1997-D Bonds were issued to advance refund<sup>13</sup> General Obligation Bonds, Series B-1 of 1997 and to fund various capital projects. There are currently no reserves in the GO 1997-D Bonds sinking fund.

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<sup>13</sup> See Section V(B)(4) – Refunding/Refinancing of Outstanding Debt.

The GO 1997-D Bonds were issued in part as Current Interest Bonds and in part as Capital Appreciation Bonds.<sup>14</sup> Interest on the Current Interest Bonds is payable on each March 15 and September 15 until maturity on September 15, 2022. Series D Capital Appreciation Bonds were issued as fully registered bonds without coupon payments in the denomination of \$5,000 maturity amount each. The Series D Capital Appreciation Bonds do not pay interest currently but accrete semi-annually, compounding interest. The GO 1997-D Bonds cannot be redeemed prior to maturity.

(c) General Obligation Refunding Notes Series F of 1997

On November 25, 1997, the City Council enacted an ordinance issuing General Obligation Refunding Notes, Series F of 1997 ("GO 1997-F Notes") in the amount of \$26,632,302.75. The GO 1997-F Notes were issued to advance refund General Obligation Bonds, Series of 1995 and to fund various capital projects. There are currently no reserves in the GO 1997-F Notes sinking fund.

The GO 1997-F Notes were issued in part as Current Interest Bonds and in part as Capital Appreciation Bonds. Interest on the Current Interest Bonds is payable on each March 15 and September 15 until maturity on September 15, 2022. Series F Capital Appreciation Notes were issued as fully registered notes without coupon payments in the denomination of \$5,000 maturity amount each. The Series F Capital Appreciation Notes do not pay interest currently but accrete semi-annually, compounding interest. The GO 1997-F Notes cannot be redeemed prior to maturity.

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<sup>14</sup> Interest payments on Current Interest Bonds are made to holders on a periodic basis while Capital Appreciation Bonds are zero coupon bonds (i.e. they accrue interest rather than pay it periodically until maturity at which time both interest and principal become due).

(d) General Obligation Notes Series A, B & C of 2003

On June 10, 2003, the City Council enacted an ordinance issuing General Obligation Notes in the Aggregate Principal Amount of \$627,800 (the "GO 2003 Notes") consisting of: (1) General Obligation Note, Series A of 2003, in an initial principal amount of \$132,800 (the "GO 2003-A Note"), (2) General Obligation Note, Series B of 2003, in an initial principal amount of \$360,000 (the "GO 2003-B Note") and (3) General Obligation Note, Series C of 2003, in an initial principal amount of \$135,000 (the "GO 2003-C Note"). The GO 2003 Notes were issued to finance a transportation infrastructure improvement project consisting of the restoration, improvement and modification of Sixth and Hamilton Streets and the intersection of State Street and SR 3014 in the City and the purchase and installation of energy saving traffic signal lenses for approximately 24 intersections in the City. In the ordinance, the City covenanted that it would include the amount of the debt service for each fiscal year in which such sums are payable, in the City's budget for that fiscal year, appropriate such amounts to the payment of such debt service, pay or cause to be paid the principal of the GO 2003 Notes and the applicable interest as due and payable and pay certain amounts into a sinking fund for each series of GO 2003 Notes. There are currently no reserves for the GO 2003 Notes in the GO 2003 Notes sinking fund.

The GO 2003-A Note bears interest at a fixed rate of 2.125% for the entire term of the GO 2003-A Note, due in 10 consecutive annual payments on or before September 1, until maturity on September 1, 2013. The GO 2003-B Note bears interest at a fixed rate of 2.125% for the entire term of the GO 2003-B Note, due in 10 consecutive annual payments on or before September 1, until maturity on September 2, 2013. The GO 2003-C Note bears interest at a fixed rate of 1.594% for the entire term of the GO

2003-C Note, due in 10 consecutive annual payments on or before September 1, until maturity on September 3, 2013. The Notes are subject to prepayment prior to maturity, at the option of the City, in whole or part, on any date.

(e) Guaranteed Revenue Note Series of 2006<sup>15</sup>

On November 28, 2006, the City Council issued an ordinance approving a project involving a City-owned three floor office building (the “Building”) to raise funds to address budgetary shortfalls. The City leased the Building to the HRA for a lump sum rental payment and the HRA subleased the Building back to the City. The HRA issued a Federally Taxable Guaranteed Revenue Note Series of 2006 (the “2006 Note”) in the amount of \$7,200,000 to finance the lump sum rental payment, the sublease and the costs of issuance.

The 2006 Note initially bore interest at a fixed rate for the first three years and currently bears interest at a variable rate which is capped at 7.5% payable on November 15 and May 15, until maturity on May 15, 2016. The 2006 Note is subject to optional redemption prior to maturity by THA, at the direction of the City, in whole or in part, at any time.

The 2006 Note is a general obligation of the City because in the ordinance, the City covenanted that in accordance with the Debt Act, it would budget and appropriate amounts from general revenues each year to cover the amounts payable under a 2006 Guaranty Agreement and pledged its full faith, credit and taxing power for any payments due under the 2006 Guaranty Agreement. Additionally, the City pledged to sell various assets, including artifacts and the City’s interest in the Harrisburg

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<sup>15</sup> Note that the “Common Features” section above does not apply to the 2006 Note.

Senators, to generate proceeds to repay the 2006 Note. There is no reserve for the 2006 Note.

Concurrently with issuance of the 2006 Note, Commerce Bank/Harrisburg, National Association ("CB"), purchased the 2006 Note for \$7,200,000. The City entered into a Guaranty Agreement with the HRA and CB (the "2006 Guaranty Agreement") to guaranty debt service on the 2006 Note. The HRA also executed an Assignment of Lease and Sublease and an Assignment of Rents and Leases whereby the HRA assigned and pledged all of its rights in the Lease and Sublease and all amounts payable to the HRA under the Lease and Sublease to CB. Additionally, the HRA executed a Leasehold Mortgage and a Security Agreement in favor of CB whereby the HRA pledged and mortgaged its leasehold interest in the Building and any fixtures in or improvements to the Building to secure payment of the 2006 Note. The City executed a Security Agreement, pledging particular artifacts and any derived proceeds to the Bank as collateral for the 2006 Guaranty.

The 2006 Guaranty Agreement provides that in the event of default of the punctual discharge of the City's obligations, the HRA or the Bank is entitled to exercise any remedies available under the Debt Act, law, equity or other statutes.

(f) General Obligation Note of 2008

On December 12, 2007, the City Council enacted an ordinance issuing the General Obligation Note of 2008 in the amount of \$2,400,000.00 (the "GO 2008 Note"). The GO 2008 Note was issued for the purpose of street repair, repaving and construction throughout the City. The GO 2008 Note was sold in a private sale by negotiation rather than a public sale to the Pennsylvania Department of Transportation (the "DOT"). In the ordinance, the City covenanted that it would include the amount of the debt service

for each fiscal year in which sums are payable in the City's budget for that fiscal year, appropriate such amounts to the payment of such debt service, pay or cause to be paid the principal of the GO 2008 Note and the applicable interest as due and payable and pay certain amounts into a sinking fund for the GO 2008 Notes.<sup>16</sup> In accordance with the Debt Act, the DOT has a security interest in all amounts deposited in the sinking funds.

The GO 2008 Note bears interest at a rate of 4.125% for the entire term of the GO 2008 Note, due in 10 consecutive annual payments on or before March 15, until maturity on March 15, 2018. The GO 2008 Note is subject to prepayment prior to maturity, at the option of the City, in whole or in part, on any date.

Note that there is no municipal bond insurance policy governing the GO 2008 Note and the SEC Rule 15c-12 reporting requirements do not apply to the GO 2008 Note.

## 2. Guaranties of THA Facility-related Debt

In addition to Harrisburg's own general obligation debt, Harrisburg has obligations relating to its guaranties of much of the debt of its authorities. Harrisburg's current financial crisis is due in large part to its obligations under the guaranties of THA's Facility-related debt, but the City has also guaranteed debt for the HPA and the HRA, among others. For a graphical representation of THA bond debt and associated guaranties and insurance, please see Section VII of this memorandum.

The annual debt service due between 2010 and 2034 ranges between \$14,643,000 and \$27,569,410, with a total outstanding principal amount remaining on the

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<sup>16</sup> The GO 2008 Note is different from the Common Features description because the City covenanted to budget debt service.

bond issues of approximately \$242 million (not including reimbursement obligations for missed interest and principal payments). On December 1, 2010, THA's Board of Directors approved the 2011 Budget for Facility Operations, which included total revenues of \$26,743,390, total operating expenses of \$21,129,484 and income prior to debt service of \$5,613,906. The debt service listed as due in 2011 includes debt payments that THA failed to make in prior years. (R.W. Beck Analysis, page 2).

Harrisburg's guaranty obligations in connection with THA's outstanding debt arise out of five indentures:

- (1) Trust Indenture, dated as of August 1, 1998 (the "1998 Indenture"), among THA and Chase Manhattan Trust Company, National Association (by succession, The Bank of New York Mellon Trust Company, National Association ("BONY")), as trustee (the "1998 Trustee");
- (2) Trust Indenture, dated as of August 15, 2002 (the "2002 Indenture"), among THA and Allfirst Bank (by succession Manufacturers and Traders Trust Company ("M&T")), as trustee (the "2002 Trustee");
- (3) Trust Indenture, dated as of June 4, 2003 (the "2003 Indenture"), among THA and Commerce Bank/Pennsylvania, National Association (by succession TD Bank, National Association ("TD Bank")), as trustee (the "2003 Trustee");
- (4) Trust Indenture, dated as of December 1, 2003 (the "Retrofit Indenture"), among THA and Commerce Bank/Pennsylvania, National Association (by succession TD Bank), as trustee (the "Retrofit Trustee"); and



- (5) Trust Indenture, dated as of December 15, 2007 (the “2007 Indenture”), among THA and Commerce Bank/Pennsylvania, National Association (by succession TD Bank), as trustee (the “2007 Trustee”).

The following table illustrates the bonds that have been issued under the respective indentures, along with their respective initial principal amounts and maturity dates:

<b>THA Facility-Related Debt</b>			
<b>Indenture</b>	<b>Series</b>	<b>Initial Principal Amount</b>	<b>Maturity Date</b>
1998 Indenture: BONY as Trustee	Guaranteed Resource Recovery Facility Refunding Revenue Bonds, Series A of 1998	\$33,110,000 (has been reduced to \$11,240,000)	September 1, 2020
2002 Indenture: M&T as Trustee	Guaranteed Federally Taxable Resource Recovery Facility Subordinate Variable Rate Revenue Notes, Series A of 2002	\$17,000,000	November 1, 2022
June 4, 2003 Indenture: TD as Trustee	Guaranteed Resource Recovery Facility Subordinate Revenue and Refunding Revenue Bonds, Series A of 2003	\$22,555,000	September 1, 2034
	Guaranteed Federally Taxable Resource Recovery Facility Subordinate Variable Rate Refunding Revenue Notes, Series B of 2003	\$29,085,000	September 1, 2034
	Guaranteed Resource Recovery Facility Subordinate Refunding Revenue Notes, Series C of 2003	\$24,285,000	September 1, 2034

THA Facility-Related Debt			
Indenture	Series	Initial Principal Amount	Maturity Date
December 1, 2003 (Retrofit) Indenture: TD as Trustee	Guaranteed Resource Recovery Facility Revenue Bonds, Series D (D-1 and D-2) of 2003	\$96,480,000	December 1, 2033
	Guaranteed Federally Taxable Resource Recovery Facility Revenue Bonds, Series E of 2003	\$14,500,000	December 1, 2011 (\$4,365,000) and December 1, 2017 (\$10,135,000)
	Guaranteed Federally Taxable Resource Recovery Facility Revenue Bonds, Series F of 2003	\$14,020,000	December 1, 2011 (\$4,205,000) and December 1, 2017 (\$9,815,000)
2007 Indenture: TD as Trustee	Guaranteed Resource Recovery Facility Limited Obligation Notes, Series C of 2007	\$20,951,574 <sup>17</sup>	December 15, 2010 <sup>18</sup>
	Guaranteed Federally Taxable Resource Recovery Facility Limited Obligation Notes, Series D of 2007	\$9,033,234 <sup>19</sup>	December 15, 2010 <sup>20</sup>
2007 Advance from Covanta to Authority		\$25,500,000	July 1, 2018

<sup>17</sup> Initial Stated Value. Note that the 2007 Indenture sometimes states that the Initial Stated Value is \$20,961,574. (p. 10).

<sup>18</sup> Neither THA nor the City made the required payment on the maturity date. The County made the payment of \$23,920,000. The City is obligated to reimburse the County for the amount pursuant to the 2007 City Guaranty Agreement (as defined below).

<sup>19</sup> Initial Stated Value.

<sup>20</sup> Neither THA nor the City made the required payment on the maturity date. The County made the payment of \$10,765,000. The City and the County are obligated to reimburse Assured for the amount pursuant to the 2007 City Guaranty Agreement (as defined below) and the 2007 County Guaranty Agreement (as defined below), respectively.

The following section summarizes the common features of each of the Facility-related bonds issued by THA. Any variation from this general description is discussed in the applicable summary for the debt issuance.

(a) Common Features

THA is required to apply all funds available, after paying reasonable and necessary operating expenses, to its debt service obligations. THA's payment obligations for the debt issued under the various indentures must be satisfied in the following order: 1998 Indenture, 2002 Indenture, 2003 Indenture, Retrofit Indenture and 2007 Indenture. In order to meet its payment obligations, THA has covenanted to charge reasonable rates for use of the Facility, but it cannot make a profit under the MAA.

Under the 1998 Indenture, a Solid Waste Revenue Fund (the "SW Revenue Fund") was created into which receipts and revenue and other amounts received by THA from any source in respect of the Facility are deposited. Money from the SW Revenue Fund is then transferred to pay operating expenses and to make debt service payments.

Each indenture established a debt service fund (a "Debt Service Fund") that is held in trust by the applicable indenture trustee. Within each Debt Service Fund, a debt service account was established (a "Debt Service Account"), within which subaccounts were created for each series of bonds or notes issued under the applicable indenture. THA is required to transfer money from the SW Revenue Fund into the applicable Debt Service Fund in an amount sufficient to make the next payment due under the applicable indenture. The applicable indenture trustee then deposits money

into the applicable Debt Service Account, which is then transferred into each subaccount.

In the event that THA were to be unable to transfer the full amount of a debt service payment into a Debt Service Account, the indentures (and the related ancillary documents) contain various mechanisms to ensure that the noteholders or bondholders will be paid in full.

Each indenture established a debt service reserve account (a "Debt Service Reserve Account") within a debt service reserve fund (a "Debt Service Reserve Fund") that would be drawn upon by the applicable indenture trustee to make debt service payments on the notes or bonds in the event of a failure of THA, the City or the County, where applicable, to make the necessary payments. On the date of issuance of the bonds or notes, a transfer was made from the SW Revenue Fund to the applicable Debt Service Reserve Account in an amount equal to applicable Debt Service Reserve Fund requirements. The amount required to be maintained in the Debt Service Reserve Account varies by indenture. In the event that there is a deficiency in a Debt Service Reserve Account, THA must repay the deficiency in not more than 12 substantially equal monthly payments after the occurrence of such deficiency.

THA also acquired municipal bond insurance policies guaranteeing the scheduled payment of principal and interest on each of the bonds or notes when due from Financial Security Assurance Inc., now by succession Assured. Assured's obligations arise only when THA, as the primary obligor, and the City and the County, where applicable, as guarantors, fail to make a scheduled payment of principal and interest on the bonds or notes when due and the applicable Debt Service Reserve Fund

and Debt Service Reserve Account are insufficient for the indenture trustee to draw upon and make the debt service payments on the bonds or notes.

With respect to THA's obligations under each indenture, the City entered into guaranty agreements (collectively, "Guaranty Agreements") with the applicable indenture trustee and THA. Under each Guaranty Agreement, the City guaranteed the full and prompt payment to the applicable indenture trustee for the benefit of the bondholders and to Assured, of the principal of, and any premium and interest on, the bonds or notes when and as such shall be due and payable. In the event of a default in payment that is required under each Guaranty Agreement, Assured, as the Directing Party, will have the right to direct remedies and actions under the applicable indenture in accordance with the terms of the indenture. In addition, in the event that an indenture trustee withdraws money from the applicable Debt Service Reserve Account and THA does not restore the balance withdrawn from the fund, the City must "forthwith" include an amount equal to the deficiency in its budget. See, e.g., the 2003 City Guaranty Agreement § 3.05. The City also agreed to include any amounts payable under each Guaranty Agreement for each fiscal year in such year's budget and to appropriate such amounts from its general revenues as may become necessary to meet its obligations under each Guaranty Agreement. The City pledged its full faith and credit and taxing power in support of these obligations.

In connection with the 2003 Retrofit Project and the 2007 Retrofit Completion Project, the County entered into a guaranty agreement whereby the County assumed a second guaranty position (behind the City and before Assured) with respect to the full and prompt payment of the principal and interest on the bonds or notes

(except the 2003F Bonds, as discussed below) when and as such shall be due and payable.

THA and the City, and in some cases the County (in connection with the 2003 Retrofit Project and the 2007 Retrofit Completion Project), also entered into Reimbursement Agreements (collectively, "Reimbursement Agreements") which provided for, among other things, their respective rights and obligations with respect to the applicable indenture and the applicable Guaranty Agreement. Under the Reimbursement Agreements, THA covenanted to pay the City or the County, as applicable, from moneys generated in connection with the Facility: (i) any amount paid by the City or the County under a guaranty plus reasonable expenses and (ii) interest on any such amount at a rate of 8%. In addition, payments by THA to the County or the City pursuant to the Reimbursement Agreements are subordinate to THA's payment of all obligations under the 1998A Bonds, the 2002 Notes, the 2003 Notes and the Retrofit Bonds.

An event of default occurs under each indenture if THA fails to make any principal or interest payment, if a receiver for the Facility is appointed, if THA fails to repair or replace any part of the Facility necessary for its efficient operation, if THA fails to observe any covenant, condition or agreement contained in the applicable indenture, if THA fails to maintain the Facility, if THA fails to comply with provisions of the Debt Act or if there is an entry of a final judgment against THA that adversely affects the control or ownership of the Facility.

There are two additional potentially important events of default under each indenture. First, an event of default under the applicable Guaranty Agreement

constitutes an event of default under the corresponding indenture. Second, an event of default occurs upon:

the institution of any proceeding without the consent or acquiescence of [THA] for the purpose of effecting a composition between [THA] and its creditors, or for the purpose of adjusting the claims of such creditors pursuant to any Federal or State statute . . . if the claims of such creditors are under any circumstances payable out of the [rates, rents, fees and charges established in connection with the operation or ownership of the Facility by [THA], any income earned on the moneys or investments on deposit in the Debt Service Fund, Debt Service Reserve Fund or any sinking or analogous fund], . . . [if THA] fails to have such proceeding withdrawn, or any order entered therein vacated or discharged, within 60 days after the institution of such proceeding or the entry of such order.

Each indenture provides for four main remedies upon an event of default.

First, the applicable indenture trustee may accelerate the payment of the bonds or notes issued under the applicable indenture. Second, the applicable indenture trustee may take appropriate judicial action for the enforcement of its rights and those of the registered owners of the relevant bonds or notes. Third, the applicable indenture trustee may take possession of and operate the Facility until all defaults have been cured. Fourth, in accordance with the Debt Act, the applicable indenture trustee may appoint a receiver. There are no cross-default provisions among the various indentures, meaning that an event of default under one indenture will not automatically cause an event of default under another indenture.

Each of the indentures provides for the acceleration of principal by the applicable indenture trustee either (a) optionally upon the occurrence and continuance of any event of default and (b) as a requirement upon the occurrence and continuance of any event of default and the written request of 25% of bondholders. In either circumstance, the trustee must obtain the consent of the directing party (the “Directing Party”), which shall be Assured so long as (a) Assured is not in default of its payment

obligations under the bond insurance policy, (b) the bond insurance policy is in effect, (c) Assured has not asserted that the bond insurance policy is not in effect and (d) Assured has not provided a written notice of waiver of its right to be the Directing Party. If Assured is ineligible to serve as the Directing Party for any of the reasons specified in (a), (b), (c) or (d) above, the City, then the County and finally 66<sup>2/3</sup>% of bondholders may be substituted as the Directing Party in that order, subject to certain conditions in the applicable indentures. The Directing Party shall have the right to direct whether to accelerate the principal (but will not have the right to direct whether to pursue other remedies).

A deficiency in a Debt Service Reserve Fund is not an automatic event of default under the applicable indenture. Such deficiency may become an event of default if it continues for 45 days after written notice from the applicable indenture trustee. If such deficiency is not capable of being remedied within 45 days after such notice, no event of default shall exist if THA commences action to cure such failure within 45 days and diligently pursues such action thereafter.<sup>21</sup> Under the indentures, the applicable indenture trustee may give the written notice of failure under the indenture in its discretion or at the request of 25% of bondholders.

(b) 1998 Financing

The following bonds were issued under the 1998 Indenture and remain outstanding: Guaranteed Resource Recovery Facility Refunding Revenue Bonds,

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<sup>21</sup> See 1998 Indenture § 8.01(h); 2002 Indenture § 8.01(h); 2003 Indenture § 8.01(h); Retrofit Indenture § 8.01(h); and 2007 Indenture § 8.01(h).



Series A of 1998, in the aggregate principal amount of \$33,110,000 (the “1998A Bonds”).<sup>22</sup> In connection with the 2003 financing (discussed in Section II(C)(1)(c) below), this amount was subsequently reduced to \$11,240,000 by an advance refunding. Payment is due to the 1998 Trustee on March 1 and September 1 of each year until maturity on September 1, 2020. The interest rate on the 1998A Bonds is 5.00%.

The amount to be maintained within the Debt Service Reserve Account of the Debt Service Reserve Fund for the 1998A Bonds is \$4,193,100, which equals the annual debt service amount for the bonds issued under the 1998 Indenture. The current Debt Service Reserve Fund balance for the 1998A Bonds is \$3,471,670.

THA acquired a municipal bond insurance policy (the “1998 Policy”) from Assured.

The City entered into a Guaranty Agreement, dated as of August 1, 1998 (the “1998 Guaranty Agreement”) with the 1998 Trustee and THA as described in the Common Features section above. The City must include any amounts payable under the 1998 Guaranty Agreement for each fiscal year, less any amount on deposit and available in the 1998 Debt Service Fund on November 1 of the previous year, in such year’s budget and appropriate such amounts from its general revenues as necessary to meet its obligations under the 1998 Guaranty Agreement. The City has not budgeted any amount for payment on the 1998 Guaranty Agreement in the 2011 budget.

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<sup>22</sup> Three additional series of bonds were issued under the 1998 Indenture, none of which remain outstanding.

THA and the City entered into a Reimbursement Agreement, dated as of August 1, 1998, the terms of which are as described in the Common Features section above.

THA failed to make the March 1, 2009 debt service payment in the amount of \$280,908 and the September 1, 2009 debt service payment in the amount of \$315,908. With respect to the March 1, 2009 payment, after deducting \$86,662 from the Debt Service Account for the 1998A Bonds, the City paid \$195,346 in accordance with its guaranty obligations. With respect to the September 1, 2009 payment, the City paid \$213,863 in accordance with its guaranty obligations. Neither THA nor the City was able to make the March 1, 2010 debt service payment in the amount of \$280,085 or the September 1, 2010 debt service payment in the amount of \$320,085; instead, such amounts were paid from the 1998 Debt Service Reserve Account.

(c) 2002 Financing

The following notes were issued under the 2002 Indenture and remain outstanding: Guaranteed Federally Taxable Resource Recovery Facility Subordinate Variable Rate Revenue Notes, Series A of 2002, in the aggregate principal amount of \$17,000,000 (the "2002 Notes"). Payment is due to the 2002 Trustee on May 1 and November 1 of each year, until maturity on November 1, 2022. The 2002 Notes have a floating interest rate which is currently at 5.72%.

On January 9, 2001, the City entered into agreements with the DEP and the EPA to, among other things, extensively retrofit the Facility so as to bring it into compliance with federal air quality regulations by June 18, 2003. The 2002 Notes were issued with the understanding that the Retrofit Bonds (defined below) could not yet be

issued, but that financing was needed for, among other things, the costs of acquiring equipment and paying design and engineering fees.

The amount to be maintained within the Debt Service Reserve Account of the Debt Service Fund for the 2002 Notes is \$800,000, which equals the annual debt service amount for the bonds issued under the 2002 Indenture. Currently, the 2002 Debt Service Reserve Fund is fully depleted.

The City entered into a Guaranty Agreement, dated as of August 15, 2002 (the “2002 Guaranty Agreement”) with the 2002 Trustee and THA, the terms of which are as described in the Common Features section above.

THA acquired a municipal bond insurance policy (the “2002 Policy”) from Assured.

THA and the City also entered into a Reimbursement Agreement, dated as of August 15, 2002.

THA failed to make the May 1, 2009 debt service payment in the amount of \$446,732 and the November 1, 2009 debt service payment in the amount of \$1,196,732. With respect to the May 1, 2009 payment, after deducting \$5,749 from the Debt Service Account for the 2002 Notes, the City paid \$440,983 in accordance with its guaranty obligations. With respect to the November 1, 2009 payment, the City was only able to pay \$395,732. The remainder, \$801,000, was transferred out of the Debt Service Reserve Fund for the 2002 Notes, depleting the 2002 Debt Service Reserve Fund. On May 1, 2010, neither THA nor the City was able to make a \$425,194 interest payment that was due on the 2002 Notes. Assured made the payment in accordance with the 2002 Policy. On November 1, 2010, neither THA nor the City was able to make a \$1,215,282 payment.

The City has not budgeted any amount for payment on the 2003 Guaranty Agreement in the 2011 budget.

(d) 2003 Financing

The following debt instruments were issued under the 2003 Indenture and remain outstanding: Guaranteed Resource Recovery Facility Subordinate Revenue and Refunding Revenue Bonds, Series A of 2003, in the aggregate principal amount of \$22,555,000 (the "2003A Bonds"), Guaranteed Federally Taxable Resource Recovery Facility Subordinate Variable Rate Refunding Revenue Notes, Series B of 2003, in the aggregate principal amount of \$29,085,000 (the "2003B Notes") and Guaranteed Resource Recovery Facility Subordinate Refunding Revenue Notes, Series C of 2003, in the aggregate principal amount of \$24,285,000 (the "2003C Notes", and, collectively with the 2003A Bonds and the 2003B Notes, the "2003 Notes"). Payment is due to the 2003 Trustee on March 1 and September 1 of each year, until maturity on September 1, 2034. The interest rates on the 2003 Notes are as follows: 2003A Bonds, 5.74% (weighted average), 2003B Notes, 5.00% currently (floating rate) and 2003C Notes, 5.00%.

The 2003 Notes were issued with the understanding that the Retrofit Project would likely be financed in late 2003, but that prior to that time a major portion of THA's outstanding debt needed to be refinanced. The proceeds of the 2003 Notes were therefore used to finance the costs of THA's working capital needs, maintain compliance with the DEP and EPA standards, purchase and cancel certain notes issued in 2000 and advance refund all outstanding 1998D Bonds.

The amount to be maintained within the Debt Service Reserve Account of the Debt Service Reserve Fund for the 2003 Notes is \$7,200,000, which equals the annual

debt service amount for the bonds issued under the 2003 Indenture. Currently, the Debt Service Reserve Fund for the 2003 Notes is fully depleted.

THA acquired a municipal bond insurance policy (the "2003 Policy") from Assured.

The City entered into a Guaranty Agreement, dated as of June 4, 2003 (the "2003 Guaranty Agreement") with the 2003 Trustee and THA.

THA and the City also entered into a Reimbursement Agreement, dated as of June 4, 2003.

THA failed to make the March 1, 2009, September 1, 2009, March 1, 2010, September 1, 2010 and March 1, 2011 debt service payments on the 2003 Notes. The City paid the March 1, 2009 debt service payment totaling \$1,742,671 in accordance with its guaranty obligations in 2009 after deducting a total of \$49,789 on deposit with the 2003 Trustee and the September 1, 2009 debt service payment totaling \$1,792,460 was paid from the Debt Service Reserve Fund. Neither THA nor the City was able to make the March 1, 2010 debt service payment totaling \$1,792,460, the September 1, 2010 debt service payment totaling \$1,633,282.77 and the March 1, 2011 debt service payment totaling \$1,401,997.30, and these amounts were paid from the Debt Service Reserve Fund.

(e) The 2003 Retrofit Project

The Retrofit Project was financed by the following bonds issued by THA which remain outstanding: Guaranteed Resource Recovery Facility Revenue Bonds, Series D, in the aggregate principal amount of \$96,480,000 (consisting of subseries D-1 in the amount of \$31,480,000 and subseries D-2 in the amount of \$65,000,000) (the "2003D Bonds"), Guaranteed Federal Taxable Resource Recovery Facility Revenue

Bonds, Series E, in the amount of \$14,500,000 (the “2003E Bonds”) and Guaranteed Federally Taxable Resource Recovery Facility Revenue Bonds, Series F, in the amount of \$14,020,000 (the “2003F Bonds”, and, collectively with the Series D Bonds and the Series E Bonds, the “Retrofit Bonds”). The 2003D Bonds bear interest at a variable rate which is pegged to a benchmark and adjusted periodically. Payment is due to the Retrofit Trustee on June 1 and December 1 of each year, until maturity as follows: 2003D Bonds (December 1, 2033); 2003E Bonds (\$4,365,000 on December 1, 2011 and \$10,135,000 on December 1, 2017); and 2003F Bonds (\$4,205,000 on December 1, 2011 and \$9,815,000 on December 1, 2017). The interest rates on the Retrofit Bonds are as follows: subseries D-1, 5.25%; subseries D-2, 5.00%; 2003E Bonds, 4.87% (weighted average); and 2003F Bonds, 4.92% (weighted average).

As described above, the Retrofit Indenture established a Debt Service Reserve Account, within which three subaccounts (the “2003D Debt Service Reserve Account,” the “2003E Debt Service Reserve Account” and the “2003F Debt Service Reserve Account”) were established for the benefit of the 2003D, 2003E and 2003F Bonds, within a Debt Service Reserve Fund (the “Retrofit Debt Service Reserve Fund”). The amount to be maintained in the 2003D Debt Service Reserve Account of the Retrofit Debt Service Reserve Fund is \$8 million. The current Retrofit Debt Service Reserve Fund balance of the 2003D Bonds is \$1,192,064.44. The amount to be maintained in the 2003E Debt Service Reserve Account of the Retrofit Debt Service Reserve Fund is \$1 million. The current Retrofit Debt Service Reserve Fund balance of the 2003E Bonds is \$270,065.26. The amount to be maintained in the 2003F Debt Service Reserve Account of the Retrofit Debt Service Reserve Fund is \$2 million (consisting of \$1 million in cash or cash equivalents and the \$1 million Reserve Policy, discussed below) (the “2003F Debt

Service Reserve Account Requirement"). Currently, the Retrofit Debt Service Reserve Fund for the 2003F Bonds is fully depleted.

The City entered into a guaranty agreement, dated as of December 1, 2003 (the "Retrofit City Guaranty Agreement") with the Retrofit Trustee, the terms of which are as described in the Common Features section above. In addition to the Guaranty Agreement terms described in the Common Features section above, the Retrofit City Guaranty Agreement obligates the City to reimburse Assured for any draw made under the Retrofit Reserve Policy.

The County entered into a Guaranty Agreement, dated as of December 1, 2003 (the "Retrofit County Guaranty Agreement"). Under the Retrofit County Guaranty Agreement, the County assumed a second guaranty position (behind the City) with respect to the full and prompt payment of principal and interest on the 2003D Bonds and the 2003E Bonds (but not the 2003F Bonds). In addition, the County is required to restore any deficiencies within the 2003D Debt Service Reserve Account and the 2003E Debt Service Reserve Account upon the failure of both THA and the City to do so.

THA acquired a municipal bond insurance policy (the "Retrofit Policy") from Assured. In addition to the terms described in the Common Features section above, Assured guaranteed the payment of Swap Obligations (defined below) when due. An additional insurance policy (the "Retrofit Reserve Policy") in the amount of \$1 million was also issued by Assured to fund the portion of the 2003F Debt Service Reserve Account Requirement not funded with cash or cash equivalents. In the event that Assured is required to make a draw under the Retrofit Reserve Policy, interest on such draw will accrue until payment of such amounts has been made to Assured.

THA, the City and the County entered into a reimbursement agreement, dated as of December 1, 2003 (the “Retrofit Reimbursement Agreement”). In addition to the Reimbursement Agreement terms described above, the Retrofit Reimbursement Agreement obligated THA to pay the County interest at the greater of the rate of 8% or the then prime rate on any amount paid by the City under the Retrofit City Guaranty Agreement or by the County under the Retrofit County Guaranty Agreement. After satisfaction of THA’s reimbursement obligation to the County, THA was obligated to pay the City from moneys generated in connection with the Facility: (i) any amount paid by the City or the County under either the Retrofit City Guaranty Agreement or the Retrofit County Guaranty Agreement, as applicable, plus reasonable expenses and (ii) interest on any such amount at a rate of 8%. The parties agreed that “if the County pursuant to the [Retrofit County Guaranty Agreement] has made a payment into the Retrofit Debt Service Reserve Account on account of a Deficiency (as defined in the [Retrofit County Guaranty Agreement]) the City’s obligation under the [Retrofit City Guaranty Agreement] to fund such Deficiency shall not be affected by such County payment, [THA] will repay to the County any such County payment out of [the Retrofit City Guaranty Agreement] [*sic*] payments to restore the Retrofit Debt Service Reserve Account when all Retrofit Indenture Funds and Accounts are fully funded, and among other remedies the County may proceed directly against [THA] and the City in any available action at law or equity to recover any Deficiency payment made by the County under the [Retrofit County Guaranty Agreement].”<sup>23</sup> Further, if the County, pursuant to the County Swap Guaranty Agreement (defined below), has made a payment under a

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<sup>23</sup> Retrofit Reimbursement Agreement, § 2(e).



Swap Agreement (defined below), the City's obligation under the City Swap Guaranty Agreement to fund such payment shall not be affected, and THA is required to repay to the County any such County payment out of the City Swap Guaranty Agreement payments and the County may proceed directly against the City for recovery under the County Swap Guaranty Agreement.

Because the 2003D Bonds are variable rate bonds, THA entered into a Qualified Interest Rate Management Agreement (the "Swap Agreement"), adopted December 15, 2003, with Royal Bank of Canada. The Swap Agreement was intended to lower net interest costs on the 2003D Bonds<sup>24</sup>. THA is obligated to pay all amounts under the Swap Agreement, including scheduled periodic payment of approximately \$800,000 in each of June and September to the Retrofit Trustee using the receipts and revenues of the incinerator ("Swap Obligations").

The City entered into a City Swap Guaranty Agreement (the "City Swap Guaranty Agreement"), dated as of December 1, 2003 among THA, the City and the Retrofit Trustee, whereby the City assumed a first guaranty position with respect to THA's Swap Obligations under the Swap Agreement. In addition, the County entered into a County Swap Guaranty Agreement, dated as of December 1, 2003, among THA, the County and the Retrofit Trustee, whereby the County assumed a secondary guaranty position with respect to THA's Swap Obligations under the Swap Agreement.

Events of default and remedies under the Retrofit Indenture are as described in the Common Features section above.

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<sup>24</sup> See Retrofit Indenture, p. 6.

Neither THA nor the City made the June 1, 2009 debt service payments for any series of the Retrofit Bonds. After crediting amounts on deposit with the Retrofit Trustee to each series of Retrofit Bonds, the Retrofit Trustee drew on the Retrofit Debt Service Funds in the amount of \$2,486,433.66 for the 2003D Bonds, \$353,027.16 for the 2003E Bonds and \$272,258.72 for the 2003F Bonds.

The City partially funded the December 1, 2009 debt service payments in amounts of \$322,794 for the 2003D Bonds, \$209,358 for the 2003E Bonds and \$202,376 for the 2003F Bonds. As a result, the Retrofit Trustee drew on the Retrofit Debt Service Reserve Funds in amounts of \$2,364,656 for the 2003D Bonds, \$746,468 for the 2003E Bonds and \$852,045 for the 2003F Bonds and, pursuant to the Retrofit County Guaranty, the County paid \$787,204 due on the 2003E Bonds. Assured paid \$630,474 due on the 2003F Bonds.

The June 1, 2010 debt service payment of \$2,687,444.84 for the 2003D Bonds was paid from the Retrofit Debt Service Reserve Fund, the payment of \$322,102.11 for the 2003E Bonds was paid by the County and the payment of \$314,743.37 for the 2003F Bonds was paid by Assured.

The December 1, 2010 debt service payments were partially paid by THA in an amount of \$938,923.09, leaving a deficiency of \$5,240,374.41. The Retrofit Trustee partially covered this deficiency by making transfers from the Retrofit Debt Service Reserve Fund totaling \$464,037. The County and Assured covered the remainder of the deficiency by making payments totaling \$3,322,142.03 and \$1,454,195.38, respectively, on the Retrofit Bonds.

In addition, THA did not make the Swap Obligation payments in the amount of \$775,652.93 due June 1, 2009 and \$818,584.93<sup>25</sup> due December 1, 2009. The County made the full June 1, 2009 payment in accordance with its obligations under the County Swap Guaranty Agreement. With respect to the December 1, 2009 payment however, as a result of a rebate made by the Retrofit Trustee to the County, the amount of the December 1, 2009 Swap Obligation paid by the County was reduced to \$720,263.33. This rebate was a result of a \$832,849.55 payment made by the City and applied pro rata to all of the City's December 1, 2009 guaranty obligations under the Retrofit Bonds and Swap Agreement.

Neither THA nor the City made a Swap Obligation payment in the amount of \$804,152.22 due June 1, 2010 and \$796,838.69 due December 1, 2010. To cover the June 1, 2010 Swap Obligation payment, the County paid \$804,151.99.<sup>26</sup> THA paid \$121,076.91 on the December 1, 2010 Swap Obligation payment and the County covered the remainder of the payment by making a payment of \$675,761.78.

(f) Covanta<sup>27</sup>

On December 31, 2006, the City's engagement as operator of the Facility concluded, and on January 2, 2007, Covanta was engaged to operate the Facility on an interim basis. Subsequently, on May 29, 2007, Covanta entered into a Management and

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<sup>25</sup> The City made a partial payment of \$832,849.55 on November 30, 2009, \$98,321.60 of which was allocated to the December 1, 2009 Swap Obligation payment. After applying this \$98,321.60 to the original December 1, 2009 Swap Obligation payment amount of \$818,584.93, the amount paid by the County was \$720,263.33. The remainder of the City's partial payment was allocated pro rata among the debt service amounts due under the 2003 Bonds.

<sup>26</sup> The remaining amount of \$0.23 was covered by cash on hand with the Retrofit Trustee.

<sup>27</sup> Note: The Common Features section does not apply to this section.

Professional Services Agreement (as amended on December 27, 2007, the “MPS”) with THA and the City whereby Covanta would provide construction and operations management services for a period of 10 years and undertake the 2007 Retrofit Completion Project.<sup>28</sup> The construction work was to be done by Covanta in accordance with a Construction Management Agreement (as amended on February 1, 2008).

Under the MPS, Covanta was obligated to advance \$25.5 million to THA for the cost necessary to undertake the 2007 Retrofit Completion Project. This advance was also used to pay an annual construction management fee to Covanta to operate the Facility. This management fee is \$875,000 per month escalated each year by the Consumer Price Index with a base year of 2007. Financial penalties are assessed and levied against the management fee for each year Covanta is unable to accept and process specified quantities of waste and steam or fails to meet the environmental standards of permits. Further, incentive compensation payments may be awarded to Covanta for each year Covanta is able to meet the environmental standards of permits and exceeds certain specified quantities of waste processing, steam and electricity sales and scrap metal sales. Payments were to be made quarterly: on January 1, April 1, July 1 and October 1 of each year. THA’s payment obligations under the MPS are subordinate to its obligations under the 1998, 2002, 2003 and Retrofit Indentures.

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<sup>28</sup> THA has retained HDR Engineering, Inc. (“HDR”) to assist with the oversight of the MPS. During the 2007 Retrofit Completion Project, HDR made periodic site visits to observe the work being performed by Covanta. Upon completion of the work, HDR observed the performance tests and reviewed the report prepared by Covanta, confirming that the contractual performance standards were achieved. For the last three years, HDR has prepared the annual consulting engineer’s report required by the trust indenture covenants and is available to perform any other consulting engineer’s services necessitated by the trust indenture covenants. (R.W. Beck Analysis, page 12).

According to the February 23, 2011 R.W. Beck Analysis, Covanta is achieving its performance obligations in the MPS. The total municipal solid waste processed by Covanta for 2010 was in excess of the specified amounts under the MPS. Covanta has also achieved its performance guaranties and R.W. Beck estimates a management fee for 2011 of \$11,424,000.

In exchange for Covanta's work and its agreement to loan \$25,500,000 to THA, Covanta negotiated for certain rights under the MPS. Importantly, Covanta has a right of first refusal in the event that THA were to sell, lease, transfer or otherwise dispose of its rights to the Facility.<sup>29</sup> THA will repay any portion of the \$25,000,000 advance that is funded from the Facility's operating revenues and related deposits and investments in various funds.<sup>30</sup> The payment obligation for the advance is subordinate to obligations under the 1998 Indenture, 2002 Indenture, the 2003 Indenture and the Retrofit Indenture<sup>31</sup> and in an event of default, Covanta may not exercise any remedies with respect to the operating revenues and related deposits and investments in various funds of the Facility, until the applicable indenture trustee has brought proceedings to exercise its rights under the applicable bond. The advance matures on July 1, 2018 and has an interest rate of 3.00%.

The City guaranteed THA's obligations to repay Covanta when and as such payments became due pursuant to a guaranty agreement dated December 14, 2007

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<sup>29</sup> MPS, page 8.

<sup>30</sup> See Section III(F)(6) – Pending Litigation Against the City. In Covanta Harrisburg, Inc. v. City of Harrisburg and Paul P. Wambach, 2010 CV 13120 (Pa. Super. Oct. 5, 2010), Covanta is seeking a judgment against the City for \$1,912,500 plus interest, attorney's fees and costs on the advance.

<sup>31</sup> MPS, Exhibit K.

(the “Covanta Guaranty Agreement”).<sup>32</sup> The City also agreed to include any amounts payable under the Covanta Guaranty Agreement for each fiscal year in such year’s budget and to appropriate such amounts from its general revenues as become necessary to meet its obligations under the Covanta Guaranty Agreement.<sup>33</sup> In support of its obligations, the City pledged its full faith, credit and taxing power. While THA’s obligation to repay Covanta is subordinated to THA’s obligation to pay amounts owing under the 1998 Indenture, the 2002 Indenture, the 2003 Indenture and the Retrofit Indenture, the City’s guaranty of THA’s obligation is general and unconditional in nature. In the event of a default in payment that is required under the Covanta Guaranty Agreement, Covanta is entitled to, among other remedies, specific performance (i.e. an order of a court requiring THA to perform a specific act) and remedies provided under the Debt Act.

The following constitute an event of default by THA under the MPS:

(1) THA breaches or fails to comply with a material provision of the MPS; (2) THA becomes insolvent; (3) THA’s “interest passes to another entity”; and (4) THA fails to make any required payment to Covanta within 10 days of such payment becoming due.

MPS § 10.

Upon an event of default under the MPS, Covanta has the right to terminate the MPS and be paid certain management and early termination fees.<sup>34</sup>

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<sup>32</sup> The County has not guaranteed THA’s obligation to repay Covanta’s \$25.5 million advance and repayment of the advance is not insured.

<sup>33</sup> The City has not included amounts payable under the Covanta Guaranty Agreement in its 2011 budget.

<sup>34</sup> Note that the Covanta Guaranty Agreement does not cover these fees.

THA made the first three scheduled repayments on the advance on July 1, 2009, October 1, 2009 and January 1, 2010, each for \$637,500. THA failed to make the April 1, 2010 payment in the amount of \$637,500, the July 1, 2010 payment in the amount of \$637,500 and the October 1, 2010 payment in the amount of \$679,794. The City also failed to make these payments but, under the Covanta Guaranty Agreement, the City's guaranty obligation for each of the April 1, 2010, July 1, 2010 and October 1, 2010 payments is limited to \$637,500.

(g) The 2007 Retrofit Completion Project

In 2007, THA determined that it was necessary to undertake the 2007 Retrofit Completion Project. THA therefore acquired financing to, among other things, fund certain working capital needs and the costs of the 2007 Retrofit Completion Project.

The following notes were issued under the 2007 Indenture and remain outstanding: Guaranteed Resource Recovery Facility Limited Obligation Notes, Series C of 2007, in an aggregate initial stated value of \$20,951,574.40<sup>35</sup> (the "2007C Notes"), and Guaranteed Federally Taxable Resource Recovery Facility Limited Obligation Notes, Series D of 2007, in an aggregate initial stated value of \$9,033,234.45 (the "2007D Notes") and, together with the 2007C Notes, the "2007 Notes"). The 2007 Notes were issued under the 2007 Indenture and matured on December 15, 2010, with a final payment due in the amount of \$34,685,000. The Series 2007 Notes bore interest at a yield to maturity of 4.5% for the 2007C Notes and 6.00% for the 2007D Notes.

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<sup>35</sup> Note that the 2007 Indenture sometimes states that the Initial Stated Value is \$20,961,574.40. (p. 10).

Like the previously described indentures, the 2007 Indenture established a Debt Service Account (the "2007 Debt Service Account") within a Debt Service Fund. On November 1, 2009, the 2007 Trustee was required to inform the City and the County of the amount on deposit in the 2007 Debt Service Account. On August 1, 2010, the 2007 Trustee informed the City of the amount on deposit in the 2007 Debt Service Account, and any deficiency was required to be deposited into the 2007 Debt Service Account by the City on or before August 15, 2010. On August 20, 2010, the Trustee was required to notify the County of any remaining deficiency, which was to be paid by the County on or before December 1, 2010. On December 15, 2010, the City was required to transfer an amount sufficient to satisfy any remaining deficiency in the 2007 Debt Service Account.

The City entered into a guaranty agreement, dated as of December 15, 2007 (the "2007 City Guaranty Agreement") with the 2007 Trustee and THA. In addition to the payment obligations described in the Common Features section above, the City also agreed to include in its 2010 budget the difference between the stated value at maturity of the 2007 Notes during any fiscal year of the City and the amount on deposit in the 2007 Notes Debt Service Account on November 1, 2009.

The County entered into a guaranty agreement, dated as of December 15, 2007 (the "2007 County Guaranty") whereby the County assumed a second guaranty position with respect to the full and prompt payment of the amounts required to pay the stated value at maturity of the 2007 Notes during any fiscal year of the City when and as such shall be due and payable.

THA, the City and the County entered into a Reimbursement Agreement, dated as of November 27, 2007.



So long as the City is in default under the 2007 City Guaranty Agreement and the County is not in default under the 2007 County Guaranty Agreement, the County will have the sole right to direct all remedies upon an event of default.

As of November 1, 2009, the City was deficient in the amount of \$34,684,998.67 on the 2007 Notes. The City failed to deposit this deficiency amount into the 2007 Debt Service Account on or before August 15, 2010, as required under the 2007 Indenture. In addition, the City was required to include the deficiency in the 2007 Debt Service Account in its budget for the 2010 fiscal year and failed to do so. The 2007 Notes matured on December 15, 2010. The City missed the payment of \$34,685,000 at maturity and the County made the full payment due at maturity.

#### D. Revenue and Assets

Harrisburg's primary General Fund revenue sources are real estate taxes, "other" taxes, which include the local services taxes and earned income taxes, departmental revenue, which includes the transfer of net profits from utility operations, and "other" revenue, which includes parking violation fines and capital fire protection appropriations.<sup>36</sup> Harrisburg's ability to generate revenue is negatively impacted by the fact that the City has 48% tax-exempt property leaving only 52% of the property subject to real estate tax.

While Harrisburg has frequently employed one-time revenue strategies to meet its near-term obligations, its recurring revenue is not projected to be sufficient to cover its recurring expenditures on an annual basis, particularly in respect of debt

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<sup>36</sup> Harrisburg 2010 Mid-Year Fiscal Report.

service obligations.<sup>37</sup> As Management Partners found, the forecast for the General Fund from 2011 to 2015 indicates a pattern of slow revenue growth and increasing expenses. The DCED has projected that property tax revenue will continue to decrease, whereas revenue from local service taxes, earned income taxes and business privilege taxes will grow at a rate near 2% per year. (DCED Consultative Evaluation at 14).

The City's parking facilities (which are held in a separate entity, the HPA) have been identified as some of Harrisburg's most valuable assets. Other potentially valuable City assets include the Facility itself, the sewage and water treatment facilities, the DeHart Reservoir and certain government buildings.

THA provides sewer and water services to citizens of Harrisburg and the County, for which it receives fees sufficient to cover its operating and debt service expenses. In addition, the Facility currently generates approximately \$5.5 million each year, primarily through tipping fees.<sup>38</sup> THA has a steam purchase agreement with NRG Energy Center Harrisburg Inc., but it does not currently have the ability to sell its steam because a necessary component is not functional.<sup>39</sup> In the past, electricity was sold to Pennsylvania Power and Light ("PP&L") in accordance with a power purchase

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<sup>37</sup> According to the DCED Consultative Evaluation, from 2004 through 2009, the City transferred significant sums of money from operations to the various Debt Service Funds in order to pay its general obligation debt. The City was able to offset some of these transfers through other financing sources such as one time sales of assets and the issuance of debt. (p. 11).

<sup>38</sup> A "tipping fee" is the charge for the unloading of waste at the Facility, measured in dollars per ton. Under the various indentures to which it is a party, THA has covenanted to maintain tipping rates at a level sufficient to cover operating expenses. See, e.g., Retrofit Indenture § 7.01. THA is also bound by Section 5607(d)(9) of the MAA not to charge rates above those that are reasonable to pay for expenses, construction, improvement, repair, maintenance and operation of its Facility, which includes debt service.

<sup>39</sup> It would cost \$500,000 to \$1 million to fix the turbines and estimated incremental revenue that would result is uncertain.

agreement that established the price paid for the power. This agreement was due to expire on December 31, 2009. Prior to expiration, in the spring of 2009, THA held meetings with PP&L and the Commonwealth to discuss their potential purchase of the Facility-generated electricity. THA hired Gabel and Associates as its energy consultant. However, PP&L subsequently notified THA that it was terminating the power purchase agreement prior to expiration. Due to weak market prices, and pursuant to the advisement of their energy consultant, THA chose not to sell the electricity under a new long-term agreement and instead currently sells power on the open market through the PJM Interconnect<sup>40</sup> using an agreement that Covanta has with the PJM Interconnect. The price paid varies hourly based on market supply and demand. Ultimately, THA intends to enter into a fixed-price power sales agreement when prices increase. (R.W. Beck Analysis, page 11).

Pursuant to a waste disposal contract dated December 1, 1993 and amended as of January 1, 2007 (due to expire in 2034), the City must require all municipal solid waste that is generated in the City and is processible at the Facility to be delivered to the Facility. (R.W. Beck Analysis, page 4). THA can raise or change rates charged to the City with at least 90 days' notice to the City of any increase or decrease in the disposal fee. Currently, the rate charged for municipal solid waste hauled from the City is \$200 per ton. (R.W. Beck Analysis, page 4).

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<sup>40</sup> PJM Interconnect is an organization that coordinates the movement of wholesale electricity in the Eastern United States power grid.

Similarly, pursuant to a waste disposal contract dated September 23, 2003 (due to expire in 2026<sup>41</sup>), the County must require all municipal solid waste that is generated in Dauphin County (with the exception of Swatara Township and Highspire Borough) to be delivered to the Facility. (R.W. Beck Analysis, page 4). Under this agreement, THA cannot unilaterally increase the rate charged to the County although there is an annual CPI adjustment. In 2008, THA suggested a rate increase for the City and the County in order to comply with its bond indenture rate covenants. The County rejected this rate increase, and an arbitrator resolved the dispute in favor of the County. As a result, the current tipping fee for the County is \$72.60. (R.W. Beck Analysis, page 4). However, according to THA, the current tipping fee is higher than the fees charged at alternative disposal facilities available to haulers collecting municipal solid waste in the County. As a result, the haulers have an economic incentive to ignore the requirement that they dispose of municipal solid waste generated within the County at the Facility. THA has been informed by some haulers that not all haulers are complying with the waste management plan requirement that all waste be delivered to the Facility, and the County has hired an inspector to investigate reported violations. Additionally, THA recently hired special counsel to investigate the flow control issue. (R.W. Beck Analysis, page 4).<sup>42</sup>

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<sup>41</sup> Note that the expiration of this contract eight years before all of the outstanding THA debt is set to be retired creates a mismatch with potentially significant consequences because the County waste represents approximately 45% of the Facility capacity (based upon 2010 municipal solid waste deliveries) and the tipping fee is above market rates. (R.W. Beck Analysis, page 5).

<sup>42</sup> Note that, to the extent THA is successful in raising County tipping fees in the future, this problem will likely be exacerbated even further.

THA also has waste disposal contracts with Cumberland County and Perry County. There are no flow control requirements for these counties and only a portion of their municipal solid waste is delivered to the Facility. Tipping fees for Cumberland County and Perry County are set by contract and adjusted annually in accordance with the CPI. As of November 2010, they were \$62.25 and \$63.50, respectively. (R.W. Beck Analysis, page 5).

In order to attract more municipal solid waste, THA has also agreed to accept waste from Schuylkill County and Northumberland County. (R.W. Beck Analysis, page 5).

In order to operate the Facility at its optimal capacity, THA also arranges for spot market waste to be delivered. THA has an agreement with a hauler to deliver municipal solid waste on an as-needed basis from transfer stations typically located in New Jersey. The agreement runs through March 31, 2011 and can be extended by mutual written consent.

THA also accepts construction and demolition waste ("C&D Waste") that it transfers within the Facility tipping buildings to long haul trailers for transport and disposal by a third-party contractor. THA currently contracts with Earthwatch Waste Systems, Inc. ("Earthwatch") for the transport and disposal services. Covanta is responsible for loading the C&D Waste into the trailers as part of its monthly fee. (R.W. Beck Analysis, page 5). The 2011 tipping fee for C&D Waste is \$74 per ton, a 5.7% increase over the 2010 tipping fee. THA anticipates paying \$49 per ton to transport and dispose of C&D Waste in 2011. (R.W. Beck Analysis, page 5).

The Facility also accepts limited quantities of special waste at higher tipping fees than the spot market rate. (R.W. Beck Analysis, page 3). These wastes are

typically wastes that require special handling at the Facility. There are physical limitations on the amount of special waste that can be received at the Facility. THA has an agreement with Chesapeake Waste Solutions, Inc. ("Chesapeake") to market THA's special waste disposal services. The agreement expires on October 31, 2011, but is automatically renewable unless notice of termination by either party is provided. THA receives, on average, \$80 per ton for special waste. (R.W. Beck Analysis, page 6).

The table below summarizes the various types and composition of municipal solid waste received at the Facility and the applicable tipping fees:<sup>43</sup>

<b>Facility Municipal Solid Waste and Tipping Fees</b>			
<b>Origin</b>	<b>Tons (2010)</b>	<b>Percent of Total</b>	<b>Tipping Fees</b>
City	37,054	13%	\$200
County	124,745	45%	\$72.60
Cumberland County	20,032	7%	\$62.25
Perry County	5,319	2%	\$63.50
Spot Market	90,473	33%	\$20
Total:	277,623	100%	

Electricity is traded daily on a regional transmission grid on a commodity basis and so prices are set by the market. THA receives approximately 4.5 cents p/kWh on average for the year. The trading process is managed by Covanta. A defect in the eighth stage blade of one turbine has impaired THA's ability to maximize the turbine's value. The cost of repair is estimated to be between \$700,000-\$800,000, and the turbine would generate an estimated \$1.2 million per year in electricity sales revenue if repaired.

The City derives a significant portion of its General Fund receipts from real property taxes. The real property tax imposed by the City in 2008 was 4.78 mills on improvements and 28.67 mills on land. Both land and improvements are assessed at

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<sup>43</sup> Table adapted from R.W. Beck Analysis, page 6.

100% of market value, with an effective combined equivalent single millage rate of 10.0898 mills.<sup>44</sup> In accordance with The Local Tax Enabling Act, Act of December 31, 1965, P.L. 1257 (as amended, the “LTEA”), the City also levies an Earned Income Tax, an Occupational Privilege Tax, a Real Estate Transfer Tax, a Business Privilege and Mercantile Tax and a Parking Tax, among others.

E. Collective Bargaining Agreements

The City is party to collective bargaining agreements on behalf of its employees with three groups, which cover approximately 90% of the total labor force: the International Association of Firefighters (through December 31, 2016), the Fraternal Order of Police (through December 31, 2015) and the American Federation of State, County and Municipal Employees (the “AFSCME”), which governs non-uniform employees (through December 31, 2014). (DCED Consultative Evaluation at 29). The DCED Consultative Evaluation notes that Harrisburg “has negotiated collective bargaining agreements that have significant, unsustainable financial impacts including pension and post retirement health care costs that are increasing at a pace far greater than the CPI”. (DCED Consultative Evaluation at 29). Like “most municipal government operations, personnel and benefit costs are the largest budget category making it difficult to adjust operations to meet available income. Without further service reductions, there is little ability to reduce expenses to meet the current revenue stream.”

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<sup>44</sup> City of Harrisburg, Pennsylvania Audited Financial Statements and Supplementary Information for the Year Ended December 31, 2008.

The collective bargaining agreements provide employees with three main benefits: guaranteed wage scales over the life of the agreement, healthcare coverage (including retiree healthcare coverage) and pension fund benefits. Pursuant to the collective bargaining agreements, the City has individual pension plans for these three groups. The Pennsylvania Municipal Retirement System (the “PMRS”) administers the firefighters plan and the AFSCME plan. M&T Bank administers the police plan. These pension plans are funded through the City’s General Fund appropriations, state aid, and employee contributions. The DCED Consultative Evaluation notes that “[f]or the most part the pension plans are overfunded and the City appears to have sufficient assets to cover the current pension liabilities . . . .” (DCED Consultative Evaluation at 25).

The Fraternal Order of Police collective bargaining agreement became effective as of January 1, 2004 and, pursuant to an amendment adopted on November 12, 2008, will remain effective through December 31, 2015 (the “FOP CBA”). Employees covered by the FOP CBA are entitled to guaranteed annual base wage increases for the term of the agreement, with a 4% wage increase as of January 1, 2011 and a 3% annual wage increase each year from 2012 through 2015. In addition to all other compensation, employees covered by the FOP CBA are entitled to receive “longevity pay”, defined as the rate of 1% of the base pay for each year of service after the employee’s third year of service up to a maximum of 13%.

Pension benefits under the FOP CBA vest after 20 years of service, and employees may begin to receive pension benefits after they reach age 50. Pension benefits gradually increase from 50% of final average salary upon 20 years of service, to a maximum of 80% of final average salary upon 27 years of service.



Active employees covered by the FOP CBA and members of their immediate families are entitled to health care coverage with the City paying 100% of the cost of such coverage. Employees who are covered by other health insurance are entitled to receive an annual payment from the City equal to \$50 per month for each month the employee elected to forego the health care coverage set forth in the FOP CBA. Retired employees covered by the FOP CBA may choose from among the City-sponsored health care coverage in effect for active employees at the time they begin to collect a pension benefit. However, employees hired prior to January 1, 1987 who retired prior to January 1, 2008 receive City-sponsored health care coverage when they vest in their pension benefits, regardless of whether they collect a pension benefit.

The International Association of Fire Fighters collective bargaining agreement became effective as of January 1, 2002 and will remain effective through December 31, 2016 (the "IAFF CBA"). Employees covered by the IAFF CBA are entitled to guaranteed annual base salary increases for the term of the agreement, with a 2% increase as of January 1, 2011, a 2% increase as of July 1, 2011, a 4% increase as of January 1, 2012 and 3% increases each year from 2013 through 2016. The IAFF CBA provides that "base salary" consists of (i) base pay plus (ii) "incentive pay" (i.e., additional payments for attainment of certifications and training) plus (iii) rank differential. Employees covered by the IAFF CBA are also entitled to receive "longevity pay" at the same rate as under the FOP CBA.

Pension benefits under the IAFF CBA vest after 10 years of service, and employees may begin to receive pension benefits after they reach age 50 with 20 years of service. An uncapped service increment of 1.25% is provided for each year of service over 20 years. Final salary is defined to include the annualized basic compensation rate

(which includes longevity pay, rank differential pay, incentive pay and premium overtime pay of one and a half times the rate of pay for all hours in excess of 40, not to exceed 104 premium hours per year, but excludes special forms of compensation such as such as shift differential, overtime pay, bonuses and severance) at the time an employee applies for benefits, or for the highest consecutive five of the 10 years prior to retirement, whichever is higher.

Active employees covered by the IAFF CBA and members of their immediate families are entitled to health care coverage in accordance with the current practice of providing such coverage.<sup>45</sup> Employees who are covered by other health insurance are entitled to receive a monthly payment from the City equal to 60% of the value of the health insurance program. Retired employees covered by the IAFF CBA, their spouses and their dependents are entitled to lifetime City-sponsored health care coverage starting at the time they begin to collect a pension benefit.

The American Federation of State, County and Municipal Employees collective bargaining agreement became effective as of January 1, 2007 and, pursuant to an amendment adopted on December 31, 2009, will remain effective through December 31, 2014 (the “AFSCME CBA”). Annual wage increases are guaranteed under the AFSCME CBA, including a 4% increase on January 1, 2011 and 3% annual wage increases each year from 2012 through 2014. In addition, effective 2011, employees covered by the AFSCME CBA are entitled to receive “longevity pay” in addition to their regular base pay salary as follows: ½% of base pay after five years of employment, 1%

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<sup>45</sup> Note: It is unclear from the IAFF CBA whether the City pays 100% of the cost of such coverage.

of base pay after 10 years of employment, 1½% of base pay after 15 years of employment and 2% of base pay after 20 years of employment.

The AFSCME CBA provides for pension benefits under two plans. Under the “A” Plan, an employee hired prior to December 30, 1974, who attains 60 years of age and 20 years of service is eligible for a “normal retirement” of 50% of his or her final average salary, defined as the annual compensation rate at the time of retirement plus longevity, shift differential and overtime or the average of the highest five consecutive years of compensation, whichever is higher. Retirees under this plan may also receive an additional 1.5% of final average salary for each year of service over 20 years. The “A” Plan also provides for a reduced pension benefit upon “early retirement”, defined as attainment of 60 years of age and 12 years of service or attainment of 55 years of age and 20 years of service.

Under the “B” Plan, an employee hired on or after December 30, 1974, or hired before December 30, 1974 who chooses benefits under the “B” Plan, “normal retirement” pension benefits may be received upon attainment of age 65 or upon attainment of age 60 and fulfilling 35 years of service. “B” Plan benefits are based on employees’ final average salary, defined as the average of annual compensation plus longevity, shift differential and overtime earned and paid during the highest three consecutive years of employment. Benefits are calculated under the “B” Plan as 2.25% of final average salary per year of service, with a maximum benefit of 75% of final average salary. The “B” Plan also provides for a reduced pension benefit upon “early retirement”, defined as attainment of 55 years of age and 10 years of service.

Active employees covered by the AFSCME CBA, their spouses and dependents are entitled to health care coverage, with employees contributing a

percentage of their base salaries toward the cost of such coverage. Such percentage ranges from 2% (for single coverage) to 6% (for four or more person coverage) of the cost of coverage. Employees who are covered by other health insurance are entitled to receive monthly payments from the City equal to \$100 per month for each month the employee elects to forego the health care coverage set forth in the AFSCME CBA. For the life of the AFSCME CBA (including extensions), the City will pay (i) 100% of the cost of health insurance for employees retiring on or after June 1, 2007, at the age of 60 with 20 years of service, and (ii) 60% of the cost of health insurance for employees retiring on or after January 1, 2002 with 20 or more years of service or at least 15 years of service at age 65. Retirees may elect to continue to cover their dependents, but they must pay the full cost of coverage for such dependents.

#### F. Pending Litigation Against the City<sup>46</sup>

The City has been named as a defendant in several litigations stemming from its guaranties of THA's Facility-related debt obligations. The following section provides a brief overview of the pending cases.

- The County of Dauphin v. The Harrisburg Authority and City of Harrisburg, 2011 CV 1618 (Pa. Super. Feb. 15, 2011): The County has filed suit against THA under the Retrofit Indenture and is seeking recovery of a Swap Obligation payment.

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<sup>46</sup> The following summary covers only litigation that is relevant to our analysis and does not cover all litigation against the City. Note that this summary reflects all documents added to the Court of Common Pleas of Dauphin County's court docket or the Commonwealth Court's court docket as applicable, as of March 30, 2011.

- The County of Dauphin and Joseph and Jacalyn Lahr v. City of Harrisburg, et al., No. 2009-CV-9271 (Pa. Super. July 22, 2009) (“Lahr 2003”): The County and the Lahrs have filed suit against the City and its elected officials under the Retrofit Indenture and is seeking a writ of mandamus pursuant to § 8261 of the Debt Act, requiring the Treasurer to apply all tax moneys first to the repayment of debt.
- The County of Dauphin and Joseph and Jacalyn Lahr v. City of Harrisburg, et al., No. 1668 C.D. 2010 (“Lahr 2007”): The County and the Lahrs have filed suit under the 2007 Indenture against the City, the Mayor, the Treasurer, the City Controller, and City Council Members. The plaintiffs are seeking specific performance of the 2007 City Guaranty Agreement and a writ of mandamus pursuant to § 8261 of the Debt Act, requiring the Treasurer to apply all tax moneys first to the repayment of debt.
- TD Bank, N.A. v. Paul P. Wambach, Treasurer of the City of Harrisburg, the City of Harrisburg, PA and The Harrisburg Authority, 2010 CV 11738 (Pa. Super. Oct. 5, 2010): TD Bank has filed suit against the Treasurer, the City and THA under the 2007 Indenture and is seeking a writ of mandamus pursuant to § 8261 of the Debt Act, requiring the Treasurer to apply all tax moneys first to the repayment of debt, a Court levy of taxes under § 8263(b)(5) of the Debt Act; appointment of a receiver under § 8264 of the Debt Act or, in the alternative, under § 5609(b)(4) of the MAA; and payment of all costs and disbursements proved at trial as additional principal due on the 2007 Notes.

- TD Bank, N.A., M&T and Assured Guaranty Municipal Corp. v. The Harrisburg Authority, the City of Harrisburg and Paul P. Wambach, Treasurer of the City of Harrisburg, 2010 CV 11737, (Pa. Super. Sept. 13, 2010): TD Bank, M&T and Assured have filed suit against THA, the City and the Treasurer under the 2002 Indenture, the 2003 Indenture, the Retrofit Indenture and the Swap Agreement. The plaintiffs are seeking judgment in the amount of unpaid debt service; an order requiring THA to charge rates sufficient to adequately cover debt service obligations; a Court levy of taxes under § 8263(b)(5) of the Debt Act; and appointment of a receiver under § 8264 of the Debt Act or, in the alternative, under § 5609(b)(4) of the MAA.
- Covanta Harrisburg, Inc. v. City of Harrisburg and Paul P. Wambach, 2010 CV 13120 (Pa. Super. Oct. 5, 2010): Covanta filed suit against the City and the Treasurer under the MPS and Covanta Guaranty Agreement. Covanta is seeking missed payments and a writ of mandamus pursuant to § 8261 of the Debt Act.
- 1. The County of Dauphin v. The Harrisburg Authority and City of Harrisburg, 2011 CV 1618 (Pa. Super. Feb. 15, 2011)

On February 15, 2011, the County filed a complaint in the Court of Common Pleas of Dauphin County, Pennsylvania against THA and the City. According to the County's complaint, on November 29, 2010, THA breached its contractual obligation under the Retrofit Bonds by failing to pay to the Retrofit Trustee the full amount of a Swap Obligation payment of \$675,761.78 due December 1, 2010. Additionally, the complaint alleges that the City, as the primary guarantor, failed to

meet its contractual obligations arising out of THA's November 29, 2010 default. As a result of THA's and the City's failure to make the required Swap Obligation payment, the County paid the balance of the Swap Obligation payment due on December 1, 2010 in the amount of \$675,761.78. Accordingly, the County is seeking judgment against THA and the City for full recovery of this amount.

On March 16, 2011, the City and THA filed separate answers to the County's complaint, that denied all the allegations above. The City and THA also asserted that the County is not entitled to bring any action under the County Swap Guaranty Agreement because Assured is entitled to control all enforcement and remedies so long as the Retrofit Policy is in effect and Assured is not in default thereunder. In addition, THA asserted a new matter that the County's claims are barred by the doctrine of prevention<sup>47</sup> because the County caused the loss of which it complains. According to THA, because the County rejected and legally contested a 2008 proposal by THA to increase the County's tipping fee in order to eliminate a projected operating deficit for 2009 of approximately \$13.5 million (including debt service), THA was prevented from raising sufficient revenue to pay its projected expenses, including its debt service. THA also alleged that the County has not complied with a requirement<sup>48</sup> that all regulated waste is to be hauled only to THA's Facility. Accordingly, the City and THA request that the Court enter judgment in their favor and award attorney's fees.

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<sup>47</sup> The prevention doctrine is a generally recognized principle of contract law according to which if a contracting party prevents or hinders fulfillment of a condition to his performance, the condition may be excused or waived.

<sup>48</sup> In 1990, the County adopted a Municipal Waste Management Plan pursuant to which all regulated waste must be transported to THA's Facility.

2. The County of Dauphin and Joseph and Jacalyn Lahr v. City of Harrisburg, et al., No. 2009-CV-9271 (Pa. Super. July 22, 2009)

(a) Summary of Suit

On March 17, 2010, the County and the Lahrs (who were subsequently joined as plaintiffs in an amended complaint<sup>49</sup>) brought suit against the City, all elected City officials (including Paul P. Wambach, treasurer of the City (the “Treasurer”)) and THA in the Court of Common Pleas of Dauphin County, Pennsylvania. On August 6, 2010, the court dismissed without prejudice the complaint in its entirety based upon standing grounds and the fact that there were adequate remedies at law, with the exception of one count of the Lahrs’ claims.<sup>50</sup>

The Lahrs’ remaining claim seeks a writ of mandamus pursuant to § 8261 of the Debt Act<sup>51</sup> requiring that the Treasurer pay from the first tax moneys or other available revenues or moneys thereafter received in the current fiscal year the amounts due on the Retrofit City Guaranty Agreement and the City Swap Guaranty Agreement. § 8261 of the Debt Act states:

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<sup>49</sup> The defendants argued in their Brief in Support of the Motion for Summary Judgment that § 8262 of the Debt Act, which prescribes remedies under the Debt Act, states that the only entities which may apply for relief under the Debt Act are “holders” of the bonds or the trustee appointed to act on the bondholders’ behalf. The Defendants argued that the County is not a “holder” of the debt and therefore may not invoke the Debt Act. The County subsequently amended its complaint to join the Lahrs as plaintiffs, stating that the Lahrs are “residents, property owners and taxpayers of the City”.

<sup>50</sup> On September 14, 2010, the County filed a motion seeking partial reconsideration of the court’s order dismissing Counts I and III of the plaintiffs’ amended complaint. The County’s motion for reconsideration was denied by an order dated October 4, 2010.

<sup>51</sup> The City argues in its brief in support of its Motion for a Stay (p. 3) that the mandamus action must be stayed because it directly conflicts with the requirements of Act 47.



If a local government unit<sup>52</sup> having outstanding any . . . guaranty of authority obligations fails or refuses to make adequate provision in its budget for any fiscal year<sup>53</sup> for the sums payable in respect of the . . . guaranty in the year or fails to appropriate or pay the moneys necessary in that year for the payment of the amount of the . . . guaranty, as the case may be, of the maturing principal of and the interest on the . . . guaranty . . . coming due in the fiscal year of the budget or for which the appropriations or payments should have been made, then at the suit of . . . any taxpayer of the local government unit, the court of common pleas shall, after a hearing held upon such notice to the local government unit as the court may direct and upon a finding of such failure or neglect, by order of mandamus require the treasurer of the local government unit to pay into the sinking fund for . . . each guaranty . . . , the first tax moneys or other available revenues or moneys thereafter received in the fiscal year by the treasurer, equally and ratably for each series for which provision has not been made in proportion to debt service for the year on . . . the amounts due upon guaranties . . . .

Accordingly, the Lahrs requested an order of mandamus requiring the Treasurer to pay the following amounts to the Retrofit Trustee from the first tax moneys or other available revenues or moneys thereafter received in the 2010 fiscal year:

- 2010 debt service on the Series D Bonds—\$5,374,900;
- 2010 debt service on the Series E Bonds—\$2,099,205;
- Replenishment of the Series D Subaccount of the Debt Service Reserve Fund—\$5,171,871.86; and
- Replenishment of the Series E Subaccount of the Debt Service Reserve Fund—\$1,000,000.

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<sup>52</sup> Harrisburg is a local government unit in accordance with section 8002 of the Debt Act, which defines “local government unit” as a “county, county institution district, city, borough . . . .”

<sup>53</sup> Note that although the Lahrs’ claim for a writ of mandamus pursuant to § 8261 of the Debt Act only specifies that the City has failed to budget and appropriate funds on amounts due in 2010 under the Retrofit City Guaranty and the City Swap Guaranty, § 8261 of the Debt Act applies to any fiscal year in which sums under a guaranty remain payable. Thus, because the City has failed to budget and appropriate funds for amounts due under the Retrofit City Guaranty and the City Swap Guaranty in its 2011 budget, the Lahrs’ potentially hold a claim for the 2011 fiscal year as well.

(b) Motion for Stay

On November 17, 2010, the City and the Treasurer filed a Motion for Stay of the trial, which was then scheduled to begin on December 16, 2010. They argued that if the writ of mandamus was issued, a preference would be given to certain creditors of the City and—because of its present fiscal circumstances—a writ of mandamus would divert funds essential to the operating budget of the City. They also argued that issuance of a writ of mandamus would subvert the Act 47 process and would thwart the development and implementation of an Act 47 Plan (as defined below) by unduly interfering with the DCED Secretary's authority and obligations under Act 47. Accordingly, they argued that the conflict between the preferential remedy of § 8261 of the Debt Act and the broader remedial program of Act 47 must be resolved by staying the proceeding.

The Lahrs argued that § 8261, by using the word “shall”, provides that the judicial remedy is mandatory when a municipality breaches its municipal debt obligations. The plaintiffs further argued that Act 47 complements, rather than conflicts with, the provisions of the Pennsylvania Constitution and the Debt Act. The plaintiffs argued that the movants' position, if accepted, would empower a court to stay any litigation against a municipality that is currently proceeding under Act 47. Accordingly, the plaintiffs sought denial of the Motion and, on December 6, 2010, the Court denied the Motion.

On January 10, 2011, the City and Treasurer filed an appeal of the December 6, 2010 order denying their Motion for Stay of the proceedings. In addition to the original arguments made by the defendants, the Renewed Motion to Dismiss or Alternatively for a Stay of the proceedings, presented a new argument for granting the

defendants' Motion. The defendants argued that the Court lacked subject matter jurisdiction because of the failure to join the Secretary, an indispensable party, since the writ of mandamus sought by the Lahrs would restrict and necessarily implicate the Secretary's "specific powers and interests" under Act 47. The defendants withdrew their Renewed Motion to Dismiss or Alternatively for a Stay on January 19, 2011. A non-jury trial was rescheduled to begin on March 15, 2011.

(c) Possibility of Appeal<sup>54</sup>

If the plaintiffs are successful, the court will enter a judgment requiring the Treasurer, pursuant to § 8261 of the Debt Act, to prioritize the amounts due on the Retrofit City Guaranty Agreement and the City Swap Guaranty Agreement from the first tax moneys or other available revenues or moneys. The City will then have 30 days to appeal such judgment. The filing of the appeal will operate as an automatic stay (or supersedeas) pending appeal against the plaintiffs' ability to obtain a mandamus order without a requirement that the political subdivision post security, subject to the right of the plaintiffs to apply to the trial or appellate court for an order requiring the political subdivision to post security in order to stay enforcement of the trial court's ruling pending appeal or to vacate the stay. See Pa. R. App. Proc. 1736-37.

Within 60 days of filing the notice of appeal, the record on appeal will be transmitted to the applicable intermediate appellate court, the Commonwealth Court or the Superior Court.<sup>55</sup> Pa. R. App. Proc. 1931. The appellant's (i.e., the person filing for

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<sup>54</sup> Note that the analysis in this section pertaining to appealing the issuance of a writ of mandamus pursuant to § 8261 of the Debt Act is also applicable to the other litigations discussed in this Section II(F) that seek such a remedy.

<sup>55</sup> There are two intermediate appellate courts in the Commonwealth—the Superior Court and the Commonwealth Court. It is unclear based on the rules governing appeals which Court is the

an appeal) main brief will be due within 40 days after the filing of the record. There will then be 30 days for the filing of an opposition by the appellee (i.e., the person who did not file for an appeal) and 14 days thereafter for the filing of a reply by the appellant. Pa. R. App. Proc. 2185. Thus, the time period between the entry of a final judgment in the trial court to the close of briefing on appeal is approximately six months. The appellate court will then typically schedule oral argument but this is at the discretion of the court. Pa. R. App. Proc. 2315. Recent statistics from the Commonwealth Court show an average time of about two months from oral argument or, if no oral argument is held, the date the court declines to set oral argument, to the court's ruling.<sup>56</sup> Thus, the total time period from entry of a final judgment in the trial court to issuance of the Commonwealth Court's ruling is likely to be about eight months. In the Superior Court, the median time in 2010 for issuance of a decision, calculated from the date the matter was first docketed, was about eleven months.<sup>57</sup> Regardless of which appellate court hears the matter, the losing party may seek permission to appeal to the Pennsylvania Supreme Court.<sup>58</sup>

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proper one to hear an appeal in this matter. It is more likely the appeal would be filed in the Commonwealth Court because one of the parties is a political subdivision. 42 Pa. C.S.A. § 762.

<sup>56</sup> Commonwealth Court of PA 2009 Statistical Report p. 2. See <http://www.aopc.org/NR/rdonlyres/FAAB37EF-DB68-4D15-BFC4-CE0A36FC7C04/0/CMWCt2009StatRpt.pdf>

<sup>57</sup> See <http://www.superior.court.state.pa.us/statistics/stats.htm>

<sup>58</sup> The appeal to the Pennsylvania Supreme Court from either the Superior Court or the Commonwealth Court would be by permission and not of right. Pa. R. App. Proc. 341(d) and 1101. In either case, it appears that the automatic stay rule would remain in effect during the pendency of the petition for leave to appeal. See 20A West's Pa. Prac., Appellate Procedure § 1736:7 (2010 ed.) (noting that this issue is not entirely settled but predicting the Pennsylvania Supreme Court would hold that the automatic supersedeas rule would apply upon the filing of a petition for allowance of appeal). This prediction is supported by a recent per curiam decision of the Pennsylvania Supreme Court. Germantown Cab. Co. v. Philadelphia Parking Auth., 2011 WL

In order to vacate the automatic stay and/or require the posting of security, the plaintiffs would have to show that (1) they are likely to prevail on the merits; (2) without the requested relief they will suffer irreparable injury; and (3) the removal of the automatic stay will not substantially harm other interested parties or adversely affect the public interest. Rickert v. Latimore Twp., 960 A.2d 912 (Pa. Cmwh. 2008), appeal denied, 973 A.2d 1008 (Pa. 2009); see also Germantown Cab Co. v. Philadelphia Parking Auth., 2011 WL 650725 (Pa. Feb. 23, 2011) (Commonwealth Court entered an order vacating the automatic stay pending a petition to appeal to the Supreme Court; on appeal to the Supreme Court from that order, the Supreme Court, citing Rickert, reversed on the basis that the Commonwealth Court's order was "not premised upon adequate evidence that Respondent would suffer irreparable harm if the supersedeas continued, or that removal of the supersedeas would not substantially harm the interested parties or adversely affect the public interest").

3. The County of Dauphin and Joseph and Jacalyn Lahr v. City of Harrisburg, et al., No. 1668 C.D. 2010

On November 9, 2009, the County filed a complaint in the Court of Common Pleas of Dauphin County against the City, the Mayor, the Treasurer, the City Controller, and City Council Members. On March 17, 2010, the County filed an amended complaint against the defendants, wherein Joseph and Jacalyn Lahr were joined as co-plaintiffs. In the amended complaint, the County alleged that it apprised the City on November 1, 2009 of a deficiency of \$34,685,000 in the 2007 Debt Service Account and requested that the amount be included in the City's budget for the year

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620725 (Pa. Feb. 23, 2011) (noting that filing of petition for allowance of appeal by parking authority "implicated the automatic supersedeas of Rule of Appellate Procedure 1736(b)").

2010.<sup>59</sup> According to the County, the City failed to budget for the deficiency or for amounts to pay obligations coming due under the 2007 Indenture in December 2010. The amended complaint requested specific performance (i.e., an order by the Court compelling the City to include the amount of the deficiency in the budget for 2010 and pay or appropriate amounts to pay the 2007 Notes on or before maturity). In the alternative, the County sought an order of mandamus by the Court, compelling the defendants to reimburse the County for its legal fees, include the amount of the deficiency in the budget for 2010 and pay or appropriate amounts to pay the 2007 Notes on or before maturity. Moreover, the amended complaint requested in the alternative if the City failed to budget or pay amounts due under the 2007 City Guaranty Agreement in the year 2010 that the Court issue an order of mandamus requiring the Treasurer to use the first tax moneys or other revenues to pay the 2007 Notes in full and reimburse the County for its legal fees.

On April 9, 2010, the defendants filed a preliminary objection to the amended complaint and a brief in support of the preliminary objection to the amended complaint. In the brief, the defendants argued that the plaintiffs' request for specific performance was inappropriate because an adequate remedy at law for breach of contract exists under the 2007 Reimbursement Agreement. Additionally, the defendants argued that the plaintiffs identified no ministerial duty<sup>60</sup> that the defendants had which

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<sup>59</sup> Note that because the 2007 Notes matured on December 15, 2010 the monthly payment of \$34,685,000 was missed by the City and was made by the County.

<sup>60</sup> A ministerial duty is one a public officer is required to perform in compliance with a mandate of legal authority upon the occurrence of certain facts. According to the defendants, the City's obligation to allocate and budget funds does not give rise to a ministerial duty because it arises pursuant to lending arrangements with various sources and is therefore based in contract.

would justify an order in mandamus and that the defendants' alleged obligation to allocate and budget funds is based on contract, which is an inappropriate basis for an action in mandamus. Furthermore, the defendants argued that any claims against the defendants must be provided for by the Debt Act but none of the plaintiffs were holders of the debt. The defendants also argued that the County's claims were not ripe because the County failed to allege any damages. The defendants furthermore argued that the Lahrs did not meet certain case law requirements for standing to bring the action.

After responsive pleadings from the plaintiffs on April 26, 2010 and by the defendants on May 3, 2010, the Court heard oral argument on the preliminary objections on June 4, 2010. On August 9, 2010, the Court entered an order dismissing the case without prejudice for the plaintiffs to seek a remedy at law. In a brief opinion, the Court explained that the plaintiffs' action seeking specific performance was dismissed because the County had adequate remedies at law through a breach of contract action once required payments were not made. The Court also indicated that the County failed to indicate ministerial duties that would warrant an order of mandamus against the defendants and that the Lahrs were not holders of the debt as required under the Debt Act and, therefore, did not have standing to request a mandamus order.

On August 16, 2010, the plaintiffs appealed the Court order to the Commonwealth Court. On November 29, 2010, the plaintiffs filed a brief in support of the appeal. In the brief, the plaintiffs argued that under the Debt Act, the City's covenant in the 2007 City Guaranty Agreement is specifically enforceable and that the County's remedy at law under contract is not adequate to enforce the City's duty to pay debt service as required by the Debt Act. Additionally, the plaintiffs argued that the trial court erred in denying plaintiffs the ability to maintain an action in mandamus and

that the County plaintiffs had standing to enforce the City's obligations under the 2007 City Guaranty Agreement.

On December 16, 2010, the Commonwealth Court granted the defendants an extension of time to file briefs in the appeal until February 2, 2011. On February 3, 2011, the defendants filed their brief. The defendants restated their original arguments from the April 9, 2010 preliminary objection, as well as a new argument that the County's and Lahrs' claims are moot because the City is now operating under a 2011 budget and the claims are seeking orders in equity or mandamus pursuant to the City's 2010 budget. Further, the defendants argued that the claims for specific performance and mandamus are moot because the maturity date of the 2007 Notes has passed and the necessary payment has been made by the County pursuant to its guaranty.

On February 17, 2011, the plaintiffs filed their reply brief. The plaintiffs restated their original arguments that the County is entitled to enforce the 2007 City Guaranty Agreement by its express terms and because of the City's failure to budget, appropriate and pay pursuant to the 2007 City Guaranty Agreement, the County is also entitled to mandamus and specific performance. In addition, the plaintiffs argued that their claims are not moot simply because the City is now operating under a 2011 budget because this would allow the defendants to avoid budgeting, appropriation and payment commitments by refusing to budget the debt obligation, and contesting litigation enforcement efforts until the year ends. Further, according to the plaintiffs, the 2007 City Guaranty Agreement provides that the City is obligated to budget, appropriate and make payment of its obligation in succeeding fiscal years if funds are



not available in the current year's budget. On March 15, 2011, THA filed an answer to the County's complaint denying all of the above allegations.

4. TD Bank, N.A. v. Paul P. Wambach, Treasurer of the City of Harrisburg, the City of Harrisburg, PA and The Harrisburg Authority, 2010 CV 11738 (Pa. Super. Oct. 5, 2010)

On September 13, 2010, TD Bank filed a complaint in the Court of Common Pleas of Dauphin County against the Treasurer, the City and THA. The complaint alleged that on October 30, 2009, TD Bank notified the City that there was a deficiency of \$34,685,000 in the 2007 Debt Service Account and requested that the amount be included in the City's budget for the year 2010. According to TD Bank, the City failed to include the amount in its budget and failed to make the payment. The complaint asserts that the County, in the exercise of its authority under the 2007 Indenture, has directed the 2007 Trustee (i.e., TD Bank) to bring suit against the City on behalf of the noteholders.

The complaint requests that the Court enter an order of mandamus, compelling the Treasurer to pay the alleged amount due under the 2007 City Guaranty Agreement from the first tax moneys or other available revenues in accordance with § 8261 of the Debt Act. Additionally, the complaint requests that the Court, following a hearing upon notice, levy taxes in an amount sufficient to satisfy the amounts allegedly due under the 2007 City Guaranty Agreement plus costs of collection. The complaint also claims that THA has failed to take any action since May of 2010 because it lacks a quorum of duly appointed members to its board. The complaint requests that the Court

appoint a receiver for THA under § 8264 of the Debt Act<sup>61</sup> or in the alternative, under § 5609 of the MAA,<sup>62</sup> that all costs and disbursements as proved at trial be deemed additional principal due on the 2007 Notes and that judgment be entered in the amount of TD Bank's expenses for bringing the action.

On October 4, 2010, THA filed a preliminary objection to the complaint. On October 22, 2010, TD Bank filed a response to the preliminary objection denying the various statements in the objection. On October 29, 2010, the City and the Treasurer filed an answer to the complaint denying the substantive allegations of the complaint. Additionally, the City and the Treasurer argued that TD Bank's claims were not ripe and that TD Bank sought mandamus of non-ministerial actions by the Treasurer contrary to Commonwealth law. Moreover, the City and the Treasurer argued that TD Bank is not a holder of the 2007 Notes and is therefore not entitled to bring a claim under the Debt Act.

On November 15, 2010, THA filed a brief in support of the preliminary objection to the complaint. In the brief, THA argued that TD Bank's request for a receiver under § 5609 of the MAA, should be dismissed because it is not ripe for decision because although a quorum does not presently exist, time still remains for THA to use its best efforts to refinance or remarket the maturing 2007 Notes in accordance with the

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<sup>61</sup> Under § 8264 of the Debt Act: "A trustee for the holders of defaulted bonds or note . . . shall be entitled as a right to the appointment, by the Court of Common Pleas, of a receiver of all or any part or parts of a project or the projects, the rents, rates, revenues, tolls and charges of which are pledged for the security of the bonds or notes of the series."

<sup>62</sup> Under § 5609 of the MAA, in the event (i) THA defaults in payment of principal or interest on a bond at maturity and the default continues for 30 days or (ii) THA fails to comply with the MAA, "[a] trustee under this subsection or a trustee under any deed of trust, indenture or other agreement, whether or not all bonds have been declared due and payable, shall be entitled to the appointment of a receiver."

terms of the 2007 Indenture.<sup>63</sup> Additionally, THA argued that the request should be denied because the MAA does not permit a receiver to engage in project financing and therefore any receiver appointed would not be able to take the action that TD Bank requests. THA also argued that TD Bank's alternative request for the appointment of a receiver under § 8264 of the Debt Act, should be dismissed because the Debt Act applies only to local government units, and as an authority, THA is not a local government unit. Additionally, THA argued that the failure of the City to make an interim payment required after a notice of deficiency does not constitute a default in debt service under the 2007 Indenture and, therefore, no remedy should be allowed as to TD Bank. Finally, THA argued that TD Bank agreed in the 2007 Indenture that its legal fees and expenses should be paid second after payment of maturity value.

On November 18, 2010, TD Bank filed a reply to the City's and the Treasurer's contentions in their October 29, 2010 answer to the complaint. TD Bank denied all of the allegations. On December 2, 2010, TD Bank filed a motion for an order of mandamus in accordance with § 8261 of the Debt Act requiring the Treasurer to pay \$34,684,998.67 out of the first moneys received by the City.

On December 10, 2010, TD Bank filed a brief in opposition to THA's preliminary objections to the complaint. In the brief, TD Bank argued that the failure of the City to pay amounts due constituted an event of default under the 2007 City Guaranty Agreement. Accordingly, TD Bank argued that under § 5609 of the MAA, TD Bank, as trustee, is entitled to appointment of a receiver if THA fails to comply with

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<sup>63</sup> Note that this argument is now moot because the 2007 Notes matured on December 15, 2010.

the MAA or defaults under the 2007 Indenture. Furthermore, TD Bank argued that even if THA is not itself subject to the Debt Act, it is a necessary party to an action seeking appointment of a receiver under the Debt Act. Additionally, TD Bank argued that the terms of the 2007 Indenture provide that a default by the City under the 2007 City Guaranty Agreement is an event of default under the 2007 Indenture and that appointment of a receiver is provided for in that instance under the terms of the 2007 Indenture.

On January 31, 2011, THA supplemented its pending preliminary objection with a supplemental preliminary objection to TD Bank's complaint. THA argued that since all the 2007 Notes matured on December 15, 2010, at which time all holders of the 2007 Notes were paid the full amount due by the County, none of the holders of the 2007 Notes have an interest in the proceedings. According to THA, there was a lack of subject matter jurisdiction because there was no longer an "actual case or controversy" and the case had been rendered moot.

On February 4, 2011, the Court entered three orders in this case. The Court's first order scheduled oral argument for February 9, 2011 on the Motion to Dismiss or Alternatively for Stay of Defendants the City of Harrisburg and Paul P. Wambach. The second order entered by the Court provided for oral argument for February 15, 2011 on THA's preliminary objections to the complaint, which was subsequently postponed to February 25, 2011. The Court also ordered a hearing for February 17, 2011 on the Motion for an Order Pursuant to §§ 8261 and 8283 of the Debt Act and for Equitable Relief, which was subsequently postponed to March 1, 2011.

On February 14, 2011, TD Bank filed preliminary objections to the supplemental preliminary objections of THA. TD Bank did not address THA's

substantive claim of mootness but, rather, argued that the Pennsylvania Rules of Civil Procedure do not provide for the filing of a “supplemental” preliminary objections. Additionally, TD Bank alleged that the facts which THA asserted rendered TD Bank’s complaint moot were not already on the record and therefore constituted a procedural violation. Accordingly, TD Bank requested that the Court dismiss THA’s supplemental preliminary objection and require THA to plead its alleged defense of mootness by filing an answer to complaint. On February 23, 2011, THA filed a response brief reiterating its argument that the case was moot for lack of subject matter jurisdiction.

On February 23, 2011, the DCED petitioned to intervene in this case pursuant to Rule 2327 of the Pennsylvania Rules of Civil procedure which permits intervention during the pendency of an action if the determination of such action may affect a legally enforceable interest of the intervenor whether or not such person may be bound by a judgment in the action. The DCED argued that it has a legally enforceable interest in developing an Act 47 Plan to relieve the City of its financial distress and in protecting the financial interests of the City and its citizens. On March 23, 2011, TD Bank responded in opposition to the DCED’s motion to intervene on the basis that the DCED has not plead any facts that give rise to a legally enforceable interest to intervene. TD Bank argued that nothing in the litigation prevents the Coordinator from meeting with creditors, negotiating and reaching a consensual resolution with creditors or proposing an Act 47 Plan. Further, TD Bank argued that under Rule 2329 of the Pennsylvania Rules of Civil Procedure, an intervention may be denied if the interest of the petitioner is already adequately represented. TD Bank argued that the City’s counsel is capable of protecting its own financial interest and those of its citizens.

On March 14, 2011, the Court entered two orders in this case. The first overruled the preliminary objections of THA and ordered THA to file its answer to the plaintiffs' complaint within 20 days of receipt of the order. The second denied THA's Motion to Dismiss or Alternatively for Stay of Defendants the City of Harrisburg and Paul P. Wambach. On March 23, 2011, THA filed a motion for clarification of the Court's March 14, 2011 order overruling its preliminary objections. THA asked the Court to clarify its March 14, 2011 order because the order did not both reference the supplemental preliminary objections or the preliminary objections and neither of these filings had been briefed. According to THA, without a ruling on its preliminary objections, THA is not obligated to file an answer to the Complaint.

On March 28, 2011, TD Bank responded in opposition to the DCED's motion to intervene by incorporating by reference its opposition filed with the Court on March 23, 2011 in TD Bank, et al. v. City of Harrisburg, et al., 2010 CV 11737, which is summarized immediately below.

5. TD Bank, N.A., M&T and Assured Guaranty Municipal Corp. v. The Harrisburg Authority, the City of Harrisburg and Paul P. Wambach, Treasurer of the City of Harrisburg, 2010 CV 11737 (Pa. Super. Sept. 13, 2010)

On September 13, 2010, TD Bank, M&T and Assured filed a complaint with the Court of Common Pleas of Dauphin County against THA, the City and the Treasurer. In the complaint, the plaintiffs alleged that THA breached the 2002 Indenture, 2003 Indenture, the Retrofit Indenture and the Swap Agreement, by failing to pay amounts due, failing to maintain the required Debt Service Reserve Fund and failing to provide in its 2010 budget sufficient funding to make the required payments. Additionally, the plaintiffs alleged that THA failed to charge rates to generate revenue sufficient to pay the debt service in connection with the financings, as

required by § 5609(b)(3) of the MAA. Accordingly, the plaintiffs alleged that under the terms of the 2002 Indenture, the 2003 Indenture and the MAA, they are entitled to a judgment in the amount of unpaid debt service and debt service reserves<sup>64</sup> and an order requiring THA to charge sufficient rates to adequately cover debt service obligations.

The plaintiffs also alleged that the City breached the 2002 Guaranty Agreement, the 2003 City Guaranty Agreement, the 2003 Retrofit City Guaranty Agreement and the City Swap Guaranty and failed to comply with the Debt Act by failing to pay amounts due under the 2002 Guaranty Agreement, the 2003 City Guaranty Agreement, the 2003 Retrofit City Guaranty Agreement and the City Swap Guaranty and by failing to provide for such payments in its budget. The plaintiffs requested that the Court enter a judgment compelling the City to fulfill these obligations. Additionally the plaintiffs requested that the Court issue an order of mandamus requiring the Treasurer to pay the amounts due under the 2002 Guaranty Agreement, the 2003 City Guaranty Agreement, the 2003 Retrofit City Guaranty Agreement and the City Swap Guaranty, out of the first tax moneys or other available revenues received and to budget for, impose and collect taxes in amounts sufficient to cover the City's obligations under the 2002 Guaranty Agreement, the 2003 City Guaranty Agreement, the 2003 Retrofit City Guaranty Agreement and the City Swap Guaranty. The plaintiffs also requested that the Court, after hearing upon notice, levy taxes to pay the amounts due under the guaranties in accordance with § 8263(b)(5) of the Debt Act.

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<sup>64</sup> Note that it is unclear based on the language in the complaint whether M&T, TD Bank and Assured are seeking for the amount of unpaid debt service reserves to be paid into the applicable Debt Service Reserve Funds or to them.

Additionally, the plaintiffs requested that the Court appoint a receiver for the Facility under § 8264 of the Debt Act or in the alternative, under § 5609(b)(4) of the MAA and enter a judgment against THA for the plaintiffs' legal fees to be paid as a first charge in accordance with § 5609 of the MAA, §§ 8264 and 8265 of the Debt Act, the 2002 Indenture, the 2003 Indenture and the Retrofit Indenture.

On October 4, 2010, THA filed a preliminary objection to the complaint. In the preliminary objection, THA argued that the bondholders and noteholders that the plaintiffs purportedly represent had been paid all debt service from guarantors and Assured and, therefore, there was no default under the indentures as to the bondholders. Accordingly, THA argued that at most, Assured could assert a claim for the amounts it had paid and its claim for a judgment and appointment of a receiver should be dismissed for legal insufficiency. Additionally, THA argued that the 2002 Indenture, the 2003 Indenture and the Retrofit Indenture provided that the plaintiffs could not take action relating to receipts and revenue of the Facility without action by the 1998 Trustee because the 1998 Indenture specifies that bondholders will not be entitled to exercise any rights or remedies with respect to receipts and revenues until and unless the 1998 Trustee institutes its rights under the 1998 Indenture. Regarding Assured's claim for payments made pursuant to the municipal bond insurance policies for the 2002 Notes, 2003 Notes, Retrofit Bonds and the Retrofit Policy, THA argued that based upon language in the 2002 Indenture, the 2003 Indenture and the Retrofit Indenture, payments required to be made by Assured are subordinate to payments made into the funds and accounts under the 1998 Indenture and thus the Court could only render a judgment which would subordinate Assured's claim to those of the holders of the 1998A Bonds. Accordingly, THA requested that the Court dismiss



the plaintiffs' complaint for failure to allege a mandatory condition precedent and for legal insufficiency. Moreover, THA argued that the plaintiffs' request that a receiver be appointed pursuant to § 8264 of the Debt Act should be dismissed because the Debt Act applies only to local government units, and as an authority, THA is not a local government unit.

On October 25, 2010, the plaintiffs filed a response to THA's preliminary objection denying the substantive statements in THA's preliminary objection. On October 29, 2010, the City and the Treasurer filed an answer to the complaint denying the allegations therein. Additionally, the City and the Treasurer contended that the plaintiffs' claims were not ripe and that the plaintiffs sought mandamus of non-ministerial actions by the Treasurer contrary to Commonwealth law. The City and the Treasurer also claimed that the plaintiffs failed to satisfy all conditions precedent before entering the complaint.

On November 8, 2010, the plaintiffs filed a motion for the appointment of a receiver under § 8264 of the Debt Act, § 5609(b)(4) of the MAA and the 2002 Indenture, the 2003 Indenture and the Retrofit Indenture. On November 9, 2010, the plaintiffs filed a motion for an order of mandamus under §§ 8261 and 8283 of the Debt Act requiring the Treasurer to pay amounts due under the 2002 Guaranty Agreement, the 2003 City Guaranty Agreement, the 2003 Retrofit City Guaranty Agreement and the City Swap Guaranty out of first tax moneys or other available revenues of the City and requiring the City to budget for any required payments under the 2002 Guaranty Agreement, the 2003 City Guaranty Agreement, the 2003 Retrofit City Guaranty Agreement and the City Swap Guaranty.

On November 15, 2010, THA filed a brief in support of its preliminary objections to the complaint reiterating the contentions in the preliminary objection. On November 23, 2010, THA filed a response to the plaintiffs' motion for the appointment of a receiver, arguing that the plaintiffs failed to cite any applicable rule or statute for the motion and that the motion is an attempt to sidestep certain procedural requirements for responding to THA's preliminary objection. On November 29, 2010, the City and the Treasurer filed a reply to the plaintiffs' motion for the appointment of a receiver, arguing that the plaintiffs' filing of the motion prior to THA having had an opportunity to answer plaintiffs' complaint, assert its defenses to the complaint or any potential claims of its own, violated procedural rules under Pennsylvania Civil Procedure. Additionally, the City noted that it had filed an application for a determination of municipal financial distress under Act 47 and that appointment of a receiver would violate the purposes of Act 47. Accordingly, the City requested that the Court stay the motion pending the distressed status determination. On November 30, 2010, the City and the Treasurer filed a reply to the plaintiffs' motion for an order of mandamus, making similar contentions.

On December 3, 2010, BONY, trustee for the 1998A Bonds, filed a petition to intervene in the case. BONY alleged that its liens under the 1998A Indenture have priority over all other liens and security interests, including any liens arising under the 2002 Indenture, the 2003 Indenture and the Retrofit Indenture. BONY noted that if its request to intervene were granted, it would file a motion on the basis of THA's defaults under the 1998 Indenture, asserting that BONY has the right to appoint a receiver for the Facility under the MAA and the 1998 Indenture and requesting that the Court appoint a receiver for the Facility.

On December 6, 2010, the plaintiffs filed a brief in opposition to THA's preliminary objections to the complaint. In the brief, the plaintiffs argued that the complaint properly pled causes of action for breach of the 2002 Indenture, the 2003 Indenture and the Retrofit Indenture. The plaintiffs further argued the fact that bondholders and noteholders were fully paid does not absolve THA from liability to them under the terms of the 2002 Indenture, the 2003 Indenture and the Retrofit Indenture. Further, the plaintiffs asserted that the MAA provides a basis for their authority to request a receiver on the basis of THA's alleged default under the 2002 Indenture, the 2003 Indenture and the Retrofit Indenture. Additionally, the plaintiffs argued that the 2002 Indenture, the 2003 Indenture and the Retrofit Indenture did not establish action by the 1998 Trustee as a condition precedent but instead restricted the ability of individual bondholders to take action against THA. Accordingly, the plaintiffs requested that the Court enter an order dismissing the preliminary objections and enter an order requiring THA to answer the complaint.

On December 23, 2010, THA filed a response to BONY's petition to intervene in the case. THA argued that THA has not breached any covenants under the 1998 Bonds and therefore, BONY has no basis or absolute right to intervene on the side of TD Bank, M&T and Assured in the case. THA requested that the Court grant THA 90 days to engage in discovery pertaining to allegations of default raised in BONY's petition and that the Court hold a subsequent hearing to determine whether BONY's intervention is appropriate.

On February 4, 2011, the Court entered four orders in this case. The first, a decree nisi, granted BONY's December 23, 2010 petition to intervene in the case. Second, the Court ordered oral argument for February 9, 2011 on the Motion to Dismiss

or Alternatively for Stay of Defendants the City of Harrisburg and Paul P. Wambach, which was subsequently postponed to February 25, 2011. Third, the Court ordered oral argument for February 15, 2011 on THA's preliminary objections to the complaint. Lastly, the Court ordered a hearing for February 17, 2011 on the Motion for an Order Pursuant to § 8261 and 8283 of the Debt Act and for Equitable Relief, which was subsequently postponed to March 1, 2011.

On February 18, 2011, BONY, as an intervenor in the case, filed a complaint against THA requesting the appointment of a receiver for the Facility under the MAA and the 1998 Indenture. BONY argued that under the 1998 Indenture, the 1998 Trustee, upon occurrence of an event of default, is entitled to appoint a receiver. According to BONY, several events of default had occurred under the 1998 Indenture, including the failure of THA to pay debt service on the 1998A Bonds of \$195,345.97 on March 1, 2009<sup>65</sup> and failure by THA to collect sufficient amounts to fund the monthly transfers of funds to the 1998 Debt Service Fund. On March 20, 2011, THA answered BONY's complaint denying each of BONY's allegations. THA argued that there had been no default under the 1998 Indenture because THA and the City made a policy decision that the City would advance the funds to make the March 1, 2009 payment rather than draw on the 1998 Debt Service Reserve Fund and cause the 1998 Debt Service Reserve Fund to suffer a loss in rate of return.

On February 23, 2011, the DCED petitioned to intervene in this case pursuant to Rule 2327 of the Pennsylvania Rules of Civil Procedure which permits intervention during the pendency of an action if the determination of such action may

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<sup>65</sup> The City made this payment pursuant to the 1998 Guaranty Agreement.

affect a legally enforceable interest of the intervenor whether or not such person may be bound by a judgment in the action. The DCED argued that it has a legally enforceable interest in developing an Act 47 Plan to relieve the City of its financial distress and in protecting the financial interests of the City and its citizens.

On February 25, 2011, the City and the Treasurer filed a brief in support of their Motion to Dismiss Or, Alternatively, for A Stay. The City and Treasurer argued that the mandamus action must be stayed because it directly conflicts with the requirements of Act 47 and the proceeding must be dismissed because the Secretary, an indispensable party, must be joined in the proceeding. This Motion was denied by the Court on March 14, 2011.

6. Covanta Harrisburg, Inc. v. City of Harrisburg and Paul P. Wambach, 2010 CV 13120 (Pa. Super. Oct. 5, 2010)

On October 5, 2010, Covanta filed a complaint in the Court of Common Pleas of Dauphin County against the City and the Treasurer seeking a judgment against the City for \$1,912,500 plus interest, attorney's fees and costs for missed payments under the Covanta Guaranty Agreement.

The complaint requests that the Court enter an order of mandamus, compelling the City and the Treasurer to budget for and apply with priority the first tax moneys and other revenues to the payments due to Covanta under the Covanta Guaranty Agreement in accordance with § 8261 of the Debt Act.

On October 25, 2010, the City and the Treasurer answered the complaint, responding that Covanta's complaint failed to state a claim upon which relief could be granted and that the mandamus claim against the Treasurer would not be ripe until the liability of THA and the City has been adjudicated. Moreover, the City and the

Treasurer argued that the mandamus claim against the Treasurer is barred by the equitable doctrines of waiver and estoppel and that the complaint seeks to compel the Treasurer to disburse funds that he has not been ordered to disburse, contrary to Commonwealth law.

On November 4, 2010, Covanta responded, denying all of the allegations in the City and the Treasurer's answer. On November 29, 2010, Covanta served upon the defendants a Request for Admissions. On January 20, 2011, Covanta filed a motion requesting that the Court determine the sufficiency of the defendants' answers to the Request for Admissions on the basis that the answers provided by defendants are evasive, incomplete and not verified. As of March 28, 2011, this case remained in discovery and the parties have filed several motions regarding the sufficiency of admissions.

#### IV. DESCRIPTIONS OF ACT 47 AND CHAPTER 9

Ordinarily, an analysis of the potential solutions to financial problems would precede an analysis of the means of achieving and implementing a solution. In this case, however, a need to understand the powers that can be brought to bear on the problems by the two means available here—Act 47 and chapter 9—and the limitations they impose on solutions, as well as the extensive public debate about them, suggest that describing those processes first may provide better context for evaluating the feasibility of possible solutions.

##### A. Act 47

Act 47 can aid a municipality in implementing various changes that could help alleviate the City's financial distress, such as improved accounting, budgeting and

taxing practices and other long-term fiscal management improvements, service delivery efficiencies and intergovernmental cooperation. However, there are a number of significant limitations to the tools it provides, particularly in its ability to bind dissenting creditors to a plan of debt adjustment.

#### 1. Basic Overview of Act 47<sup>66</sup>

Act 47 is intended to foster the fiscal integrity of municipalities so that the health, safety and welfare of the citizens of each municipality, and of the Commonwealth, is protected. Act 47 § 102. According to the DCED, Act 47 directs the Commonwealth to provide oversight and to develop a formal partnership with municipalities that are experiencing financial distress to ensure that citizens receive vital services. Accordingly, the Commonwealth will provide fiscal management, technical assistance and financial aid to a distressed municipality and will seek long-term fiscal management improvements, service delivery efficiencies, intergovernmental cooperation and economic/community development activities.<sup>67</sup>

##### (a) The Appointment of a Coordinator

Within 30 days after a determination that a municipality is financially “distressed”, the DCED must appoint a plan coordinator (the “Coordinator”) to prepare a plan to address the City’s financial distress (the “Act 47 Plan”). Act 47 § 221(a). As

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<sup>66</sup> For a timeline of key Act 47 events, please see Section VIII of this memorandum.

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[http://www.google.com/url?sa=t&source=web&cd=11&ved=0CBYQFjAAOAo&url=http://www.governor.state.pa.us/portal/server.pt/document/1022455/dced\\_secretary\\_says\\_harrisburg\\_is\\_financially\\_distressed\\_under\\_act\\_47\\_pdf&rct=j&q=Act%2047%20directs%20the%20commonwealth%20to%20provide%20oversight%20and%20to%20develop%20a%20formal%20partnership&ei=5heKTZ\\_fK8yL0QHjo5HrDQ&usg=AFQjCNEgt3SSkz\\_4ZOI3izUDlqXB9UmKlw](http://www.google.com/url?sa=t&source=web&cd=11&ved=0CBYQFjAAOAo&url=http://www.governor.state.pa.us/portal/server.pt/document/1022455/dced_secretary_says_harrisburg_is_financially_distressed_under_act_47_pdf&rct=j&q=Act%2047%20directs%20the%20commonwealth%20to%20provide%20oversight%20and%20to%20develop%20a%20formal%20partnership&ei=5heKTZ_fK8yL0QHjo5HrDQ&usg=AFQjCNEgt3SSkz_4ZOI3izUDlqXB9UmKlw).

noted above, on January 12, 2010, the DCED appointed Novak, S&L, the PEL and O'Donnell as the Coordinator.

Once appointed, the Coordinator is granted full access to municipal records. Act 47 § 222. In addition, the municipality is required to provide the Coordinator routinely with data that is relevant to the municipality's recovery effort, which will likely include information about material management, administrative and financial decisions made by the municipality, whether or not such decisions directly relate to the recovery effort. The Coordinator's principal role is to develop the Act 47 Plan.

(b) Act 47 Plan Contents

The Act 47 Plan must, under § 241(2), include recommendations that will, if relevant to the cause of a municipality's distressed status:

“(i) Satisfy judgments, past due accounts payable, and past due and payable payroll and fringe benefits;

(ii) Eliminate deficits and deficit funds;

(iii) Restore to special fund accounts money from those accounts that was used for purposes other than those specifically authorized;

(iv) Balance the budget, avoid future deficits in funds and maintain current payments of payroll, fringe benefits and accounts through possible revenue enhancement recommendations, including tax or fee changes;

(v) Avoid a fiscal emergency condition in the future;

(vi) Enhance the ability of the municipality to negotiate new general obligation bonds, lease rental debt, funded debt and tax and revenue anticipation borrowing;

(vii) Consider changes in accounting and automation procedures for the financial benefit of the municipality; and

(viii) Propose a reduction of debt due on specific claims by an amortized or lump-sum payment considered to be the most



reasonable disposition of each claim possible for the municipality considering the totality of circumstances.”

The Coordinator’s Act 47 Plan may also include or recommend, if relevant:

- possible changes in collective bargaining agreements, in permanent or temporary staffing levels or in the municipality’s organization;
- recommended changes in municipal ordinances or rules or for special audits or further studies;
- a capital budget to address infrastructure deficiencies;
- recommendations for greater use of the Commonwealth’s economic and community development programs; and
- an analysis of whether a chapter 9 case could assist the municipality.

Act 47 § 241.

(c) Development of an Act 47 Plan

The Coordinator must develop an Act 47 Plan and deliver it for public inspection within 90 days after an executed contract between the DCED and the Coordinator. Act 47 § 242(a). We understand that a contract with the Coordinator has not yet been executed; however, Frederick Reddig, the Executive Director of the Governor’s Center for Local Government Services, has advised us that the Coordinator’s Act 47 Plan is nevertheless expected to be delivered on approximately June 1, 2011, before the statutory deadline. The Coordinator will typically meet with members of the municipality’s city council,<sup>68</sup> community leaders, union leadership and other individuals to ensure that the Coordinator has as much information as possible to formulate the

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<sup>68</sup> Act 47 commonly makes reference to the “governing body”, which is defined as “the council in cities.” Act 47 § 103. Accordingly, this memorandum will reference the City Council when Act 47’s provisions reference the “governing body”.

Act 47 Plan. Section 223(a) of Act 47 provides that the Coordinator “may hold public meetings as defined in [the Sunshine Act] in connection with plan preparation.”

Within 15 days after the Coordinator files the Act 47 Plan with the City Clerk, written comments on the plan may be filed with the Coordinator. Act 47 § 242(d). Within 20 days after the filing date, the Coordinator must hold a public meeting to receive comments on the Act 47 Plan. Act 47 § 242(e). The Coordinator must invite the Mayor and City Council Members to attend the public meeting. Id. The Coordinator may revise the Act 47 Plan based on any comments received or on his own initiative within 10 days after the public meeting. Act 47 §§ 243(e), 244. Neither the Mayor nor the City Council may revise the Coordinator’s Act 47 Plan, although the Coordinator must consult with them if the Coordinator revises the Act 47 Plan and must give consideration to comments they may propose. Act 47 § 244.

Within 25 days after the Coordinator’s public meeting, the City Council must enact an ordinance approving implementation of the Act 47 Plan, including enactment of necessary related ordinances and revisions to existing ordinances, or reject the Act 47 Plan. If the City Council approves the Act 47 Plan, the Mayor<sup>69</sup> may issue an order directing the implementation of the Act 47 Plan within seven days after the enactment of the ordinance. Act 47 § 245. The Coordinator is charged with implementing the Act 47 Plan. Act 47 § 247(a).

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<sup>69</sup> Act 47 commonly makes reference to the “chief executive officer”, which is defined as the “mayor in a mayor-council form of government . . . of a city operating under an optional form of government pursuant to the act of July 15, 1957 (P.L. 901, No. 399), known as the Optional Third Class City Charter Law.” Harrisburg is organized under the Optional Third Class City Charter Law—Mayor-Council Plan A. Accordingly, this memorandum will reference the Mayor when Act 47’s provisions reference the “chief executive officer”.

If the City Council rejects the Act 47 Plan (or if the Mayor refuses or fails to issue an order directing the implementation of the Act 47 Plan within seven days after enactment of an ordinance), the Mayor then has 14 days to develop an alternative Act 47 Plan, including a signed order implementing it. Act 47 § 246. Act 47 does not appear to contain specific requirements for the contents of an Act 47 Plan developed by the Mayor; however, the intent of Act 47 is likely that the requirements of an Act 47 Plan developed by the Mayor mirror those of an Act 47 Plan developed by the Coordinator. In any case, a Mayor's Act 47 Plan would be subject to the approval of the City Council and the DCED Secretary. Following a public hearing on the Mayor's plan, the City Council may enact an ordinance approving the Mayor's Act 47 Plan. Act 47 § 246(c).

If the City Council does so, the DCED Secretary must review the alternative plan to determine whether its implementation will overcome the municipality's financial problems. Act 47 § 246(d)(1). If the DCED Secretary determines that the Act 47 Plan will not do so, or if the City Council has not approved the Mayor's Act 47 Plan, the Coordinator must notify the municipality that he is requesting the DCED Secretary to suspend Commonwealth funding to the municipality. Act 47 §§ 248, 264(a). The municipality has 10 days to respond to show why funding should not be suspended. Act 47 § 264(b). If the DCED Secretary and Coordinator are not satisfied with the explanation, the DCED Secretary, within 20 days of the Coordinator's request, shall certify to the municipality in writing that each grant, loan, entitlement or payment by the Commonwealth or any of its agencies shall be suspended pending adoption of an Act 47 Plan calculated to fully resolve the municipality's financial distress. Act 47 § 264(c). Suspended funds shall be held in escrow by the Commonwealth until the DCED Secretary has rescinded the certification. Id. The only exceptions to the funding

suspension are for funds for capital projects already under contract, disaster relief funds, pension fund disbursements and emergency grants and loans provided under section 302 of Act 47. Act 47 §§ 251(b), 246(d)(3).

(d) Implementation of the Act 47 Plan

If the Coordinator's Act 47 Plan is enacted, the Coordinator is responsible for its implementation, which means that the Coordinator oversees, controls (or delegate control of) and monitors the implementation process. Act 47 § 247(a). If the Mayor's alternative Act 47 Plan is approved by the City Council and the DCED Secretary, then the Mayor is responsible for its implementation. Act 47 § 247(b).

(e) Termination of Distressed Status

A municipality's distressed status may be terminated only upon a determination by the DCED Secretary that the conditions which led to the original distressed determination are no longer present. Act 47 § 253(a). A municipality may petition the DCED Secretary to make such determination. Act 47 § 253(b). To determine whether the conditions that led to the original distressed determination are no longer present, the DCED Secretary considers whether: (1) monthly reports submitted by the Coordinator to the DCED indicate that the termination of the distressed status is appropriate; (2) accrued deficits in the municipality have been eliminated; (3) obligations issued to finance all or part of the municipality's deficit have been retired; and (4) the municipality has operated, for a period of at least one year, under a positive current operating fund balance or equity, as evidenced by the municipality's audited financial statements prepared in accordance with generally accepted accounting principles. Act 47 § 253(c).

## 2. Selected Precedent Act 47 Cases

Twenty-six Commonwealth municipalities have been designated as distressed by the DCED and have participated in the Act 47 rehabilitation process. These precedents may provide guidance as to the potential substance and utility of Harrisburg's Act 47 Plan.

### (a) City of Reading

The City of Reading's ("Reading") Act 47 plan, which was filed with Reading's City Clerk on May 28, 2010, included a comprehensive analysis of the causes of its financial problems as well as prescribed remedies designed to address those problems. Inefficiency was identified as one of the principal causes of Reading's troubles. Accordingly, Reading's Act 47 plan called for restructuring the fire department and combining certain similar governmental units, such as the Parks and Property Maintenance units with the Department of Public Works. Additionally, the Act 47 plan established a formal performance measurement process in order to ensure that information was being properly tracked.

Reading's Act 47 plan also imposed certain requirements designed to curtail unnecessary spending. For example, in order to contain fast-growing employee compensation, Reading's Act 47 plan included, for both non-represented managers and union workers alike, a three-year base wage and step freeze; a restructuring of health benefits, including increased employee contributions to monthly premium costs; and overtime and premium pay reductions. Additionally, Reading's Act 47 plan provided that all new labor agreements between the city and the unions representing its employees for calendar years 2010-2014 must not contain certain provisions, including any new overtime or premium pay benefits or requirements or any increase in existing

overtime or premium pay benefits or requirements. Under its Act 47 plan, Reading also sought to stop paying retirement benefits in excess of those allowed by the Third Class City Code and to restructure certain health benefits.

In addition, Reading's Act 47 plan included a revenue package that would allow it to meet its short-term and long-term needs. The package featured temporary increases in resident and non-resident taxes<sup>70</sup>, increased contributions from Reading's parking and water authorities and called for a 10% property tax increase that will become effective in 2014.<sup>71</sup>

(b) City of Pittsburgh

The City of Pittsburgh's ("Pittsburgh") Act 47 plan, which was filed with Pittsburgh's city clerk on June 11, 2004, was developed after a detailed review of Pittsburgh's finances and recurring deficits. The major elements of Pittsburgh's Act 47 plan were to streamline operations (which included a 15% across-the-board cut in the budgets for the mayor, the city council, the clerk and the city controller), contain a growing employee compensation expense (which included a two-year wage freeze), strengthen financial management practices and strategic investment in long-term fiscal health and develop new revenue streams. For instance, Pittsburgh's Act 47 plan directs the city to secure contributions of at least \$6 million annually from the nonprofit community beginning in 2011. This may be achieved through increased voluntary

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<sup>70</sup> Reading's Act 47 plan proposed specific gradual step downs in the tax rates over the subsequent four years and said it was "intended that additional marginal resident EIT rate reductions would be enacted in subsequent years." (p. 273). Reading's Act 47 plan also proposed gradual stepdowns and an elimination of non-resident earned income tax entirely by 2014.

<sup>71</sup> If the city is able to exceed its projected financial performance, it would have the ability to moderate the 2014 property tax increase or further reduce the resident earned income tax that year. (p. 7).

contributions through a revised agreement with the Public Service Fund through the Pittsburgh Foundation, pursuing General Assembly approval for amendments to the payroll preparation tax to include nonprofit institutions, or initiating new legally enforceable fees applicable to services rendered to tax-exempt institutions. (p. 21).

(c) Westfall Township

Westfall Township is the only municipality in the Commonwealth's history to have filed for chapter 9. Westfall Township filed directly for bankruptcy protection without first going through the Act 47 process and became deemed "distressed" under Act 47 as a result. The DCED stated that it supported Westfall Township's bankruptcy petition because the community's public services were under "imminent jeopardy" because a \$20 million judgment would have wiped out the township's budget.<sup>72</sup> As required under section 263(b) of Act 47, the Coordinator worked jointly with the bankruptcy court to expedite the formulation, confirmation and adoption of a chapter 9 plan.

Westfall Township filed for chapter 9 protection on April 10, 2009 after a \$20 million federal judgment was entered in favor of a real estate developer. As part of a settlement, the dollar amounts otherwise owed by Westfall Township to the Katzes under the judgment were set aside by the settlement and replaced with the amount of \$6 million without interest, payable in 80 quarterly installments of \$75,000 each, due and payable to the Katzes on March 31, June 30, September 30 and December 31 of each year beginning on September 30, 2009. If Westfall Township fails to comply with the terms,

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<sup>72</sup> <http://thetimes-tribune.com/news/westfall-twp-s-first-in-the-state-bankruptcy-may-not-be-pennsylvania-s-last-1.695242#axzz1HRn5ImVH>.

obligations and duties of the settlement, then the monetary amount owed to the Katzes will revert to in excess of \$21 million. Westfall Township was required by the chapter 9 plan to construct certain sewage facilities needed by the developer. Under the chapter 9 plan and the Act 47 plan, Westfall Township agreed to levy a special property tax millage beginning in 2010 at rates necessary to meet certain cash and construction obligations until fully satisfied. The plans also required Westfall Township: (1) to seek authority to levy increases on general fund millage; (2) to pursue and complete a loan in the amount of \$125,000 to meet a cash flow deficit resulting from legal fees incurred in the litigation and related bankruptcy proceedings; and (3) to proceed with a request for proposals for a Tax and Revenue Anticipation Note in 2010.

(d) City of New Castle

The City of New Castle ("New Castle") filed its Act 47 plan on July 18, 2007. The Act 47 plan addressed the primary causes of New Castle's financial distress—pension fund deficits and recurring annual operating budget deficits—through significant changes designed to control expenditures, boost revenues and improve service delivery to New Castle.

New Castle's Act 47 plan's cost control measures are mostly aimed at reducing expenditures for personnel services, wages, healthcare coverage and other employee compensation. To improve New Castle's administrative and management resources, new positions in finance, accounting, benefit coordination and information technology were created under the plan and the plan recommended that a committee be established to explore a change from a Mayor-Council to a Council-Manager form of



government.<sup>73</sup> To control personnel service expenses, the plan set out new guidelines for restructuring wages and salaries, premium payments (e.g., overtime, shift differential), healthcare, pension plans and paid leave.

New Castle's Act 47 plan contains measures aimed at boosting revenues including improved tax collection and cost recovery. New Castle's Act 47 plan suggested several strategies for increasing tax collection such as outsourcing delinquent and current tax collection for LTEA taxes, reviewing tax-exempt properties for development opportunities and establishing a foundation to generate contributions from nonprofit institutions. Cost recovery initiatives included charging organizations receiving special police patrol coverage for the cost of overhead and employee benefits, establishing fees to cover inspection services and increasing parking fines. New Castle's Act 47 plan also included resident and non-resident earned income tax and property tax increases. The increases are to be slowly phased out as expenditure control initiatives take effect and other revenue sources grow.

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<sup>73</sup> The Commonwealth creates and regulates all Pennsylvania towns and cities. The authority and power vested in the City is derived from the state. Harrisburg is a "Third Class City" and operates under the Third Class City Code. The citizens of Harrisburg have chosen to organize the city government under the Optional Third Class City Chart Law—Mayor-Council Plan A. This is often referred to as a strong mayor form of government. In a mayor-council government, there is typically a separation of powers between the directly elected mayor and the city council, with the mayor having executive powers and the city council having legislative powers. In the council-manager form of government, by contrast, the city council typically oversees the general administration, makes policy and sets the budget. The city council typically hires a city manager to carry out the day-to-day administrative operations of the city and often the mayor is chosen from among the council on a rotating basis. See [http://www.nlc.org/about\\_cities/cities\\_101/163.aspx](http://www.nlc.org/about_cities/cities_101/163.aspx).

### 3. Analysis of the Act 47 Option

As outlined above, Act 47 provides a distressed municipality with several tools. Below is an analysis of the potential benefits and shortcomings of these tools as they relate to Harrisburg.

#### (a) Comprehensive Review of the City

Once appointed, the Coordinator undertakes a comprehensive review of a distressed city's financial and operational structure and may recommend changes that could help alleviate the city's financial distress. A review could benefit Harrisburg by providing a complete look from the perspective of a neutral third party with experience in municipal administration and finance at the ways in which the City could become more fiscally sound.

#### (b) Priority Consideration for Development Programs

Municipalities that have been declared distressed are given priority in all economic and community development programs funded by the Commonwealth, as long as the Coordinator determines that the funding is consistent with the efforts to alleviate the municipality's financial crisis. Act 47 § 282.

#### (c) Grants and Loans

DCED maintains a fund under Act 47 to provide grants and loans, including emergency loans, to municipalities that have been declared distressed on an interest-free basis. Act 47 § 301. Where a municipality has been designated distressed but before final adoption of an Act 47 plan, the municipality or the Coordinator may apply to the DCED for an expedited loan or grant to assist the municipality immediately if the applicant verifies that either: (1) the municipality is in imminent danger of insolvency or (2) there is a clear and present danger to the health and safety of residents

of the municipality. Act 47 § 302(b). The municipality may make such an application by the municipality's city council enacting a resolution. 16 Pa. Code § 36.6(i)(2). After receipt of an application, the DCED Secretary must review all data immediately available and determine whether emergency funds are warranted. The DCED Secretary or the applicant may request a hearing to provide additional evidence of emergency need, which must be held within 15 days from the date the application is received. An emergency loan shall come due within nine months from the date of the loan. Based upon a detailed analysis of the municipality's financial condition, the Coordinator's Act 47 Plan may recommend conversion of all or a part of an emergency loan to a long-term loan. 16 Pa. Code § 36.6.

After a municipality has adopted an Act 47 plan, the mayor or a person designated by the municipality's city council may apply to the DCED Secretary for a grant or loan. The DCED will give priority to grant applications that include plans for activities that are intended to accomplish the following: (1) reduce municipal costs; (2) share municipal services; (3) improve municipal productivity; (4) increase municipal revenues; and (5) ease and assist the municipality through consolidation or merger. 16 Pa. Code § 36.7(a). A municipality may apply for a grant by adopting a resolution authorizing the governing body to apply for the grant. 16 Pa. Code § 36.7(c). If the DCED determines that a long-term loan is appropriate, the municipality must enact an ordinance allowing it to incur indebtedness, which must pledge the municipality's full faith, credit and taxing power to satisfy the obligation incurred under the ordinance. 16 Pa. Code §§ 36.6(i)(3)-(4).

Any funds received from a loan or grant under Act 47 may be used solely for the payment of current expenses of the municipality. Act 47 § 303(a). Moreover, the

DCED Secretary is not permitted to approve an application to any one municipality for an amount which will substantially impair the DCED's ability to distribute the remaining sum fairly and equitably to other applicants or potential applicants. Act 47 § 303(c). The DCED currently has approximately \$3.15 million<sup>74</sup> appropriated to carry out the provisions of Act 47. Given the magnitude of the City's outstanding obligations and budget issues, it is unlikely that this tool could have a meaningful impact on the City's financial condition.

(d) Encourages Negotiation with Creditors

The Act 47 process encourages distressed municipalities to negotiate with their creditors. Creditors who do not consent to the handling of their claim under an Act 47 plan (for example, if the Act 47 plan proposes to pay less than the full amount of the principal of such creditor's claim) must notify the Coordinator that they reject the Act 47 plan. Act 47 § 243(a). The Coordinator will then preside over negotiations between the municipality and the dissenting creditors. Act 47 § 243(c). However, because Act 47 does not provide for nonconsensual debt adjustment, a power that is available in specified circumstances in a chapter 9 case, the City might not have as much direct bargaining power in these negotiations as it would in a chapter 9 case where the City as a chapter 9 debtor might be able to force on its creditors a reduction of their claims. Nor can the Coordinator require creditors to participate. Therefore, a successful

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<sup>74</sup> There was \$3.15 million available in the Act 47 fund at the end of January 2011. These funds are used to hire Coordinators, develop Act 47 plans and provide low interest loans and must be shared with the 19 other municipalities currently designated as "distressed" by the DCED. The amount available in the Act 47 fund fluctuates over time as revenue comes in on account of loan repayments and as payments are sent out.

Act 47 resolution requires unanimous consent by all creditors whose rights will be affected.

(e) Ability to Increase Tax Rates

After a municipality has adopted an Act 47 plan, it may petition the Court of Common Pleas of the county where it is located to raise earned income,<sup>75</sup> real property<sup>76</sup> or both tax rates above statutory limits. Act 47 § 123(c)(1). Any such tax increase will be effective for one year. Act 47 § 123(c)(2). The Court may extend the municipality's ability to exceed these statutory limits annually until the termination date of the municipality's Act 47 plan. Act 47 § 141(a).

(f) Prospective Collective Bargaining Agreements Limitations

Although a municipality must continue to comply with its existing collective bargaining agreements in a non-bankruptcy context, Act 47 enables a municipality to limit the terms of prospective collective bargaining agreements. An Act 47 plan may recommend possible changes in collective bargaining agreements, Act 47 § 241(3), and any collective bargaining agreement executed after the adoption of an Act 47 plan may not in any manner violate, expand or diminish the Act 47 plan's provisions. Act 47 § 252. For example, Reading had collective bargaining agreements set to expire shortly after its Act 47 plan was adopted, and these restrictions applied to the renegotiated collective bargaining agreements. Reading's Act 47 plan prohibited it from entering into new collective bargaining agreements that contained any new

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<sup>75</sup> The statutory limit for earned income tax is one percent. LTEA Section 8(3).

<sup>76</sup> The statutory limit for real property is 25 mills (a mill is equal to one-tenth of a cent), with an additional 5 mills available with court approval. Court approval is to be granted if the taxing body shows the additional millage is necessary to meet the needs of an approved budget. Third Class City Code § 2531(5).

overtime or premium pay benefits, any new benefits for retirees or other inactive employees and any additional pay for time not worked and imposed other related restrictions.

Although Act 47 could assist Harrisburg in its negotiation of future collective bargaining agreements, this assistance may be insufficient to alleviate Harrisburg's financial distress because Harrisburg would still be required to meet its obligations under its current collective bargaining agreements until their expiration in 2014 and 2015. The DCED Consultative Evaluation notes that Harrisburg's existing collective bargaining agreements "have significant, unsustainable financial impacts including pension and post retirement health care costs that are increasing at a pace far greater than the CPI." (DCED Consultative Evaluation at 29). Unless the union counterparties voluntarily agree to renegotiate the terms of these collective bargaining agreements, Act 47 will not reduce the financial obligations that the collective bargaining agreements impose through the expiration of their current terms.

(g) Timing

An Act 47 plan can require an extended amount of time to implement, and a municipality may receive continuing benefits while under Act 47, so most municipalities stay under the protection of Act 47 for many years. The following table illustrates the average amount of time that the municipalities that have been designated as "distressed" under Act 47 have remained designated as "distressed".

Pennsylvania Municipalities in Act 47					
	Municipality	Distressed Determination Date	Distress Determination Rescission	Years to Rescission	Years (if still distressed)
1	City of Farrell, Mercer County	November 12, 1987			23

Pennsylvania Municipalities in Act 47					
	Municipality	Distressed Determination Date	Distress Determination Rescission	Years to Rescission	Years (if still distressed)
2	City of Aliquippa, Beaver County	December 22, 1987			23
3	City of Clairton, Allegheny County	January 19, 1988			
4	Borough of Wilkinsburg, Allegheny County	January 19, 1988	November 10, 1998	10	
5	Borough of Shenandoah, Schuylkill County	May 20, 1988	April 16, 1993	4	
6	Borough of Braddock, Allegheny County	June 15, 1988			22
7	Borough of Franklin, Cambria County	July 26, 1988			22
8	Borough of Rankin, Allegheny County	January 9, 1989			22
9	Borough of Ambridge, Beaver County	April 10, 1990	April 16, 1993	3	
10	City of Duquesne, Allegheny County	June 20, 1991			19
11	City of Scranton, Lackawanna County	January 10, 1992			19
12	City of Johnstown, Cambria County	August 21, 1992			18
13	Borough of East Pittsburgh, Allegheny County	November 13, 1992	December 27, 1999	7	
14	Borough of Millbourne, Delaware County	January 7, 1993			18
15	Borough of Homestead, Allegheny County	March 22, 1993	March 28, 2007	14	
16	City of Chester, Delaware County	April 6, 1995			15
17	Borough of North Braddock, Allegheny County	May 22, 1995	April 11, 2003	7	
18	Borough of Greenville, Mercer County	May 8, 2002			8
19	Borough of West Hazleton, Luzerne County	March 27, 2003			7
20	City of Pittsburgh, Allegheny County	December 29, 2003			7

Pennsylvania Municipalities in Act 47					
	Municipality	Distressed Determination Date	Distress Determination Rescission	Years to Rescission	Years (if still distressed)
21	Township of Plymouth, Luzerne County	July 27, 2004			6
22	City of Nanticoke, Luzerne County	May 26, 2006			4
23	City of New Castle, Lawrence County	January 5, 2007			4
24	Westfall Township, Pike County	April 14, 2009			1
25	City of Reading, Berks County	November 12, 2009			1
26	City of Harrisburg, PA	December 15, 2010			—

20	Municipalities Still In “Distressed” Status	<u>Average Years:</u>	8	13
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There are 20 municipalities currently designated as distressed under Act 47 (including Harrisburg). Only six municipalities have emerged from distressed status, and none have done so in less than three years. In fact, the average amount of time spent being designated as “distressed” for those municipalities which have had their distressed status terminated is eight years; for municipalities which continue to be designated “distressed”, the average is 13 years. Accordingly, although the adoption of an Act 47 Plan must occur quickly, Act 47 is not a “quick fix”, and there is a concern that municipalities may come to rely unduly on the protections of distressed status as a crutch rather than addressing their underlying structural problems. These continuing benefits of remaining in Act 47 include the ability to raise certain taxes above prescribed statutory caps and to receive priority for certain grants and loans.

If Harrisburg were to file a chapter 9 petition, the bankruptcy court would likely require that the City develop and seek confirmation of a plan of debt adjustment in a timely manner. Yet although the adjustment of the City’s debt would be



immediate upon exit from bankruptcy, other aspects of the Chapter 9 Plan (as defined below) would be implemented over time, as would be the case for the Act 47 Plan.

(h) Lack of Restructuring Tools

Act 47 does not provide municipalities with many of the reorganization tools available to municipalities under chapter 9. For instance, Act 47 lacks provisions that (1) expressly halt creditor enforcement actions against the City (such as the various mandamus actions described above); (2) bind dissenting creditors to accept less than 100% of the amount of, or make any other adjustment to, their claims; (3) grant the City a discharge of debt comparable to the type of discharge available under chapter 9; (4) permit the City to avoid and recover certain transfers from the City to third parties; or (5) permit the City unilaterally to reject executory contracts and leases, including collective bargaining agreements. Instead, the only incentive that Act 47 provides is the ability to block the municipality from receiving funding from the Commonwealth or any of its agencies if no Act 47 Plan is adopted or implemented. Act 47 § 248. This is a blunt instrument that only indirectly exerts pressure on the municipality's creditors and is primarily targeted only at the municipality itself.

B. Certain Potential State Actions

1. State Takeover of the City

Under Section 32 of the Pennsylvania Constitution, the General Assembly may “pass no local or special law in any case which has been or can be provided for by general law and specifically the General Assembly shall not pass any local or special law regulating the affairs of cities.” Section 32 is thus a state constitutional prohibition against interference with local government and enactment of special legislation affecting only one or a few municipal governmental units. Nevertheless, as long as compliance

with state procedures is voluntary and the municipality has the option of rejecting any plan proposed by the state, the Commonwealth may enact legislative devices that, while not entirely supplanting governance of the City, effectively put aside the City's governance structure. The following section discusses one such example of state legislation, the Pennsylvania Intergovernmental Cooperation Authority ("PICA").

## 2. PICA

In 1991, Philadelphia was on the verge of bankruptcy. Between 1950 and 1990, Philadelphia had lost 25% of its population and 27% (250,000) of its jobs. Between 1970 to 1990, median household income had dropped 22% adjusted for inflation from \$31,600 to \$24,600. These changes were caused by deindustrialization, the loss of well-paying factory jobs and ineffective government policies such as the failure of the minimum wage to keep pace with inflation.<sup>77</sup> As a result, Philadelphia had accumulated hundreds of millions of dollars in budget deficits resulting in declining bond and credit ratings. City services were deteriorating—Philadelphia had suspended its pension payments to its pension fund, and it was unclear whether Philadelphia would be able to pay its workers.

In response to Philadelphia's situation, the legislature enacted the Pennsylvania Intergovernmental Cooperation Authority Act for Cities of the First Class (P.L. 9, No. 6), 53 P.S. 12720.101 et seq., as amended (the "PICA Act") for the purpose of providing financial assistance to the City of Philadelphia ("Philadelphia") in overcoming a severe financial crisis. The PICA Act created a seven member authority (the "PICA")

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<sup>77</sup> Marc Breslow, Miracle in Philadelphia: Can fiscal management really save the cities?, Dollars & Sense, July 17, 1997.

Authority”) with five voting and two ex officio, non-voting members (the state’s budget director and the finance director of Philadelphia) with several powers and duties, including:

- (1) To assist cities in avoiding defaults, eliminating and financing deficits, maintaining sound budgetary practices and avoiding the interruption of municipal services;
- (2) To borrow money and issue bonds to assist cities;
- (3) To negotiate intergovernmental cooperation agreements with cities containing such terms and conditions as will enable such cities to eliminate and avoid deficits, maintain sound budgetary practices and avoid interruption of municipal services;
- (4) To provide financial assistance, including loans and grants, to assist cities upon such terms and conditions as may be approved by a qualified majority of the board or as may be specified by the General Assembly to eliminate or prevent deficits of a city; and
- (5) To exercise, while any bonds issued by the PICA Authority to assist the city remain outstanding, powers of review concerning the budgetary and fiscal affairs of that city consistent with this act and the city’s home rule charter or other optional plan of government.

The PICA Authority wielded its greatest influence through its power to issue bonds on behalf of Philadelphia and to make the proceeds available to Philadelphia. As a precondition for receiving the PICA funds and, thus, money from PICA bonds as well as other state grant funds, Philadelphia was required to create a five-year financial plan, updated each year. The plan had to be approved by the PICA Authority and had to provide a detailed written description of the revenues and obligations of Philadelphia and contain proposals for cutting costs citywide and in each department (a section each on Personnel and Philadelphia’s Workforce, the Capital Budget, Debt and Management, and Productivity).

In its original review of Philadelphia’s first five-year financial plan, the PICA Authority cited problems, and required changes, in items such as the following:

(1) lack of detailed explanation of the methods used to project revenues and deficits; (2) inconsistent estimates of the size and uses of the initial proposed PICA borrowings; (3) a proposed debt service reserve fund larger than the Internal Revenue Service allows; (4) a proposed \$119 million borrowing to refinance four bond issues that were not included in the plan's overall borrowing status; and (5) a mission report on Philadelphia's estimates of wage and benefit levels for municipal employees, which the PICA Authority said it needed to review how labor agreements are incorporated into the plan.<sup>78</sup>

In the PICA Authority's first year, it borrowed about \$475 million in Special Tax Revenue Bonds on behalf of Philadelphia. Philadelphia used these bond proceeds to fund its cumulative deficit, current and later year deficits and certain capital projects and productive enhancement initiatives. Philadelphia in turn accepted a one percent increase in sales tax on goods sold within Philadelphia and agreed to divert a part of Philadelphia's wage tax to repay the PICA debt.

Under the PICA Authority's guidance, Philadelphia also cut labor costs by negotiating with Philadelphia's municipal unions. An agreement with PICA obligated the Philadelphia mayor to advise PICA before approving any labor contracts or any other expenditures that would exceed \$1 million, giving PICA a powerful influence over labor contracts. Philadelphia won new contracts and froze wages for almost three years and cut benefits despite a brief strike and an unsuccessful union

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<sup>78</sup> Steven Dickson, Bond Buyer, March 12, 1992.

action before the Pennsylvania Supreme Court challenging PICA's constitutionality.<sup>79</sup> Philadelphia also collected back taxes, improved efficiency in city services such as trash removal and slashed budgets by eliminating close to 1,500 jobs.

Further, the PICA Authority exercised its oversight functions to ensure continued compliance and progress with the financial plan. According to Ronald G. Harry, PICA's first executive director: "When [Philadelphia] reports its performance on the plan, we examine [Philadelphia's] methodology and execution--how is it managing the plan. We see if [Philadelphia] is being honest with itself. The [Philadelphia] mayor and the [Philadelphia] city council provide a quarterly report [required] by statute within 45 days of the closing quarter. A line-by-line examination can be done . . . . There cannot be a variance of more than one percent on a net projected end-of-year basis."<sup>80</sup> The right to review Philadelphia's five-year budget annually and the right to audit virtually every branch of Philadelphia government to assure itself that Philadelphia was sticking to the plan appears to have had a significant disciplining force on Philadelphia.

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<sup>79</sup> The unions challenged the constitutionality of PICA primarily on two grounds. First, the unions claimed that PICA violated the Pennsylvania Constitution because the PICA Authority was unconstitutionally appointed. The unions alleged that because four of the members of the PICA Authority are appointed by the legislature and only one by the governor, this violated separation of powers by placing the executive powers of the board in the hands of the legislative branch of government. The Court dismissed this first claim for lack of standing because the unions failed to show how their interests are affected by the means in which the board members were appointed. Second, the unions alleged that PICA constituted a "special commission" in violation of Article III, Section 31 of the United States Constitution. The Court rejected this second argument and held that PICA did not interfere with the municipal government of Philadelphia because the City had voluntarily sought assistance and entered into cooperation with the PICA Authority and Article IX, Section 5 of the United States Constitution enables the City to enter into such agreement. The Court thus dismissed the second claim. Local 22 v. Commonwealth, 613 A.2d 522 (Pa. 1992).

<sup>80</sup> Barbara Ettore, Management Review, April 1993.

The PICA Act created a vehicle through which all funding came into Philadelphia, effectively limiting the Philadelphia city council's and mayor's ability to govern outside the PICA framework. Legislative devices such as the PICA Act, while not entirely supplanting governance of a city, can effectively put aside a city's governance structure.

### C. Chapter 9

#### 1. Chapter 9 of the Bankruptcy Code

Chapter 9 of the Bankruptcy Code offers protection from creditor collection actions, permits the rejection of executory contracts and provides an opportunity to adjust the City's debts through an established framework that contemplates the ability to adjust the City's debts by, and bind all creditors (including dissenting creditors) to, a plan of debt adjustment (a "Chapter 9 Plan"). A Chapter 9 Plan provides a final resolution and restructuring of all claims against the "debtor" (i.e., the City). The description below addresses only those chapter 9 provisions that we believe would be most relevant if Harrisburg were to file a chapter 9 case. For a timeline of key bankruptcy events, please see Section IX of this memorandum.

#### (a) Commencement of a Chapter 9 Case

##### (i) Eligibility

The Bankruptcy Code imposes six eligibility requirements for a municipality to use chapter 9. All six must be satisfied.

##### a. "Municipality"

Only a "municipality" may file for relief under chapter 9. 11 U.S.C. § 109(c)(1). The term "municipality" is defined in the Bankruptcy Code as a "political subdivision or public agency or instrumentality of a State." 11 U.S.C. § 101(40). As a

third class city of the Commonwealth, Harrisburg meets the Bankruptcy Code's definition of a municipality.

b. State Authorization

A municipality must be "specifically authorized, in its capacity as a municipality or by name, to be a debtor under [chapter 9] by State law, or by a governmental officer or organization empowered by State law to authorize such entity to be a debtor . . . ." 11 U.S.C. § 109(c)(2). Act 47 provides distressed municipalities with the specific authorization required by the Bankruptcy Code to file a chapter 9 petition, so long as one of the following conditions is present:

- (1) After recommendation by the Coordinator pursuant to section 241(6);
- (2) 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;
- (3) One or more creditors of the municipality have rejected the proposed or adopted Act 47 Plan, and efforts to negotiate resolution of their claims have been unsuccessful for a 10 day period;
- (4) A condition substantially affecting the municipality's financial distress is potentially solvable only by utilizing a remedy exclusively available to the municipality through chapter 9; or
- (5) A majority of the current or immediately preceding governing body of a municipality determined to be financially distressed has failed to adopt a plan or to carry out the recommendations of the Coordinator pursuant to Act 47.

Act 47 § 261(a). Under Act 47, this authority to file for chapter 9 must be exercised by a majority vote of the City Council. Act 47 § 261(b). The bankruptcy court will resolve any challenge to whether Harrisburg is specifically authorized to file. See In re New York City Off-Track Betting Corp., 427 B.R. 256 (Bankr. S.D.N.Y. 2010).

Whether Harrisburg meets the specific authorization requirement would depend on the facts as they existed when a chapter 9 petition was filed. If the Coordinator's Act 47 Plan recommends filing a chapter 9 case, the first criterion would be satisfied. If a creditor is successful in obtaining an unstayed mandamus remedy against the City, the second criterion would be satisfied. If a creditor does not accept an Act 47 Plan that calls for adjustment of the creditor's claim, the third criterion would be satisfied. Whether the fourth criterion is satisfied will depend on circumstances at the time of the filing. If the City Council does not adopt an Act 47 Plan or fails to carry out the recommendations of the Coordinator pursuant to Act 47, the fifth criterion would be satisfied.

c. Insolvency

A municipality must be "insolvent", as the Bankruptcy Code defines that term, to be eligible to file a chapter 9 case. 11 U.S.C. § 109(c)(3). A municipality is "insolvent" when the municipality is "(i) generally not paying its debts as they become due . . . ; or (ii) unable to pay its debts as they become due." 11 U.S.C. § 101(32)(C). "Generally not paying" is not defined in the Bankruptcy Code, but the Bankruptcy Code uses the same phrase in the section establishing the requirements for a creditor to file an involuntary bankruptcy petition against a non-municipal debtor. 11 U.S.C. § 303(h)(1).

Courts have adopted a "totality of the circumstances" test for determining whether a debtor is generally not paying its debts as that term is used in section 303(h)(1). See In re Vortex Fishing Sys., 277 F.3d 1057 (9th Cir. 2001); General Trading Inc. v. Yale Materials Handling Corp., 119 F.3d 1485 (11th Cir. 1997); In re Concrete Pumping Servs., 943 F.2d 627 (6th Cir. 1991); In re All Media Props, Inc., 5 B.R. 126, 147-148 (Bankr. S.D. Tex. 1980), aff'd, 646 F.2d 193 (5th Cir. 1981). The leading



bankruptcy treatise notes that “[d]espite a wide range of definitions among the courts, there is a general consensus that the determination of ‘generally not paying’ should employ a multifactor test. It is a factual, as distinguished from legal, determination. There is no single mathematical formula that can be used to determine whether the standard has or has not been met. The diversity exhibited by those suffering financial distress calls for a broad definition rather than a mechanical test.” 6 Collier on Bankruptcy ¶ 303.31 (Alan N. Resnick & Henry J. Sommer eds. 16th ed. 2010). “The concept of ‘generally’ is a comparative one. The question is how many debts are being paid in proportion to the total number of debts. Not paying one debt out of a sizable number of debts does not satisfy the ‘generally’ in the ‘generally not paying’ standard. . . . On the other hand, failing to pay one significant creditor can satisfy the standard.” 6 Collier on Bankruptcy ¶ 303.31[1] (Alan N. Resnick & Henry J. Sommer eds. 16th ed. 2010). “Where a debtor fails to pay even one debt that makes up a substantial portion of its overall liability, a court may find that he is generally not paying his debts.” *In re Amanat*, 321 B.R. 30, 39-40 (Bankr. S.D.N.Y. 2005).

In fashioning an appropriate test, courts have considered several different factors.

One approach is to undertake a rough calculus of the number and amount of the alleged debtor's delinquent and current debts on the petition date. The results determine whether the ratio of delinquent current debts is supportive of a pattern of ‘generally not paying.’ For example, a court could first determine which debts a debtor was paying and which debts it was not paying, excluding debts subject to bona fide disputes from the calculation. It could then compare the number and the amount of unpaid debts with the number and amount of paid debts, factoring in the materiality of the debtor's nonpayment as well as the debtor's general conduct of its financial affairs. Another articulation of the standard is to look at the totality of the circumstances existing when the petition is filed and consider the proportion of the debt being paid—both in terms of the proportion of creditors being paid and the proportion

of the debt, in dollar value being paid. Some courts also suggest looking at how the debtor conducted its financial affairs. . . . Another formulation of this standard requires a court to examine whether a debtor has regularly missed a significant number of payments to creditors or has regularly missed payments which are significant in amount in relation to the size of the debtor's operation.

6 Collier on Bankruptcy ¶ 303.31[2] (Alan N. Resnick & Henry J. Sommer eds. 16th ed. 2010) (internal quotations omitted).

We believe that the City meets the “generally not paying” definition of insolvency, because it has repeatedly failed to pay its debts under certain of its guaranties of THA debt as they have become due.<sup>81</sup> The magnitude of THA debt is sufficiently large that it dwarfs the City's other liabilities. The amount that is currently past due, inclusive of payments that were made from Debt Service Reserve Accounts is \$64,889,423.<sup>82</sup> The City has not included any Facility-related debt service payments in its 2011 budget.<sup>83</sup> Accordingly, we believe that a court would find that the City is generally not paying its debts as they become due. Because the insolvency test is in the alternative (“generally not paying” or “unable to pay”), the City would not have to address ability to pay—a less certain standard given the potential universe of possible actions a municipality could take to potentially be able to pay a debt—as a condition to showing that it is “insolvent”.

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<sup>81</sup> Creditors opposed to a chapter 9 filing may argue that the City has missed only interest payments and limited principal payments, all of which is small relative to the City's overall obligation on THA debt, and that the remainder of the debt has not yet become due.

<sup>82</sup> A&M Assessment, page 51.

<sup>83</sup> See [http://www.harrisburgpa.gov/Downloads/Budgets/2011\\_pro\\_debt\\_service.pdf](http://www.harrisburgpa.gov/Downloads/Budgets/2011_pro_debt_service.pdf).

d. Desire to Effect a Plan to Adjust Its Debts

A municipality must also establish that it desires to effect a plan to adjust its debts. 11 U.S.C. § 109(c)(4). This requirement is designed to ensure that the chapter 9 petition is intended to result in a chapter 9 plan under which creditors' claims will be adjusted and is not being filed for an improper purpose.<sup>84</sup>

e. Pre-negotiation Requirement

Typically the most difficult requirement to meet, a municipality must show that it has made an attempt to achieve a consensual resolution of its obligations, unless there are exigent circumstances. Section 109(c)(5) of the Bankruptcy Code requires as an eligibility condition that the municipality:

- (1) has obtained the agreement of creditors holding at least a majority in amount of the claims of each class that the debtor intends to "impair" (i.e., to alter the legal, equitable or contractual rights in any way) under a chapter 9 plan;
- (2) has negotiated in good faith with creditors and failed 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 chapter 9 plan;
- (3) is unable to negotiate with creditors because such negotiation was impracticable; or
- (4) reasonably believes that a creditor may attempt to obtain a "preference".<sup>85</sup>

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<sup>84</sup> Examples of an improper purpose include filing to harass or to cause unnecessary delay or needless increase in the cost of litigation. Fed. R. Bankr. P. 9011.

<sup>85</sup> A "preference" is a payment or other transfer by the debtor to or for the benefit of a creditor for an already existing debt made while the debtor was insolvent.

A negotiation with Harrisburg's creditors would likely involve a limited number of parties. Although the bondholders of THA Facility-related debt have a claim for future payment by the City if THA misses such payment, a consensual deal with the County, Assured and Covanta could be sufficient to address the City's Facility-related debt problems. The bondholders should be indifferent as to whether they are paid by the City or by the County or by Assured. Accordingly, if the City were able to reach a consensual out-of-court resolution with the County, Assured and Covanta over the reimbursement obligations of the City to them, the bondholders should be neutral, because they will continue to be paid in full, and a chapter 9 case would therefore be unnecessary.<sup>86</sup> If, however, Harrisburg is not able to reach an agreement, then to be eligible to file a chapter 9 case, it must show that it negotiated in good faith with at least its principal creditors and failed to reach agreement or that such negotiation is impracticable or that it reasonably believed that a creditor may attempt to obtain a preference.

Whether Harrisburg can meet the third alternative—that negotiation is impracticable—remains an open question. The answer to this question will depend on external factors and later events. A recent precedent reads “impracticable” according to its ordinary meaning of “incapable of being performed or accomplished by the means employed or at command; infeasible”. In re Valley Health System, 383 B.R. 156, 163 (Bankr. C.D. Cal. 2008), quoting Webster's New International Dictionary 1136 (3d ed. 2002), rejects any notion that the impracticability requirement applies only where

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<sup>86</sup> Note that, as a technical matter, it might still be useful for a bankruptcy court to approve the arrangement to resolve any “technical default” issues on the City's Guaranty Agreements.

creditors are too numerous for negotiations. Id. at 162. See generally 2 Collier on Bankruptcy ¶ 109.04[3][e][iii] (Alan N. Resnick & Henry J. Sommer, eds. 16th ed. 2010). Similarly, negotiation may be impracticable with one group of creditors where negotiations with another key group have hit an impasse. In re Vills. at Castle Rock Metro. Dist. No. 4, 145 B.R. 76, 85 (Bankr. D. Colo. 1990); In re Pierce County Hous. Auth., 414 B.R. 702, 714 (Bankr. W.D. Wash. 2009). Negotiations may be equally impracticable where another part of the financial equation—a viable long-term financial plan based on revenues or expenses—cannot be determined. Thus, where a city was unable, despite extended negotiations, to reach agreement with its labor unions over labor costs, which constituted the largest portion of the city’s budget, “it would have been futile to negotiate with other creditors.” In re City of Vallejo, 408 B.R. 280, 298 (9th Cir. B.A.P. 2009).

Alternatively, to meet the fourth alternative, Harrisburg may show that it reasonably believed that a creditor may attempt to obtain a preference. The creditors currently seeking mandamus are the principal Facility-related THA creditors. If the City does not reach an agreement with the principal creditors, whether through an Act 47 Plan or otherwise, the mandamus actions are likely to proceed onward. If a creditor is successful in obtaining an unstayed mandamus remedy against the City, the fourth alternative under the pre-negotiation requirement should be satisfied.<sup>87</sup> However, satisfaction of the fourth alternative does not necessarily satisfy the good faith requirement, discussed immediately below.

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<sup>87</sup> Note that the fourth alternative may be currently satisfied based on the remedies sought in the pending litigations.

f. Good Faith

In addition to the eligibility requirements in section 109(c), section 921(c) requires that a petition must be filed in “good faith”. The Bankruptcy Code does not define “good faith”. Courts have determined, however, that the primary function of the good faith requirement in section 921(c) is “to ensure the integrity of the reorganization process by limiting access to its protection to those situations for which it was intended.” In re Sullivan County Reg’l Refuse Disposal Dist., 165 B.R. 60, 80 (Bankr. D.N.H. 1994). To determine whether a petition is filed in good faith, courts may evaluate “(i) the debtor’s subjective beliefs; (ii) whether the debtor’s financial problems fall within the situations contemplated by chapter 9; (iii) whether the debtor filed its chapter 9 petition for reasons consistent with the purposes of chapter 9; (iv) the extent of the debtor’s prepetition negotiations, if practicable; (v) the extent that alternatives to chapter 9 were considered; and (vi) the scope and nature of the debtor’s financial problems.” In re Pierce County Hous. Auth., 414 B.R. 702, 714 (Bankr. W.D. Wa. 2009) (citing 6 Collier on Bankruptcy ¶ 921.04[2] (Alan N. Resnick & Henry J. Sommer eds. 16th ed. 2010)).

g. Burden of Proof

If Harrisburg files a chapter 9 petition, some creditors may challenge its eligibility to file. If so, Harrisburg will bear the burden of establishing that it does in fact meet the eligibility requirements. In re City of Vallejo, 408 B.R. 280, 289 (B.A.P. 9th Cir. 2009) (quoting In re Valley Health Sys., 383 B.R. 156, 161 (Bankr. C.D. Cal. 2008)); In re County of Orange, 183 B.R. 594, 599 (Bankr. C.D. Cal. 1995) (quoting In re City of Bridgeport, 129 B.R. 332, 339 (Bankr. D. Conn. 1991)). If the court determines that the municipality meets all of the eligibility requirements, the court then issues an “order for

relief”, which is a court order determining that the City is eligible to be a chapter 9 debtor.

(ii) Governing Body Vote

The City Council has the power to authorize a chapter 9 petition. Act 47 § 261(b). In doing so, it must determine that at least one of the conditions listed in Section 261(a) of Act 47 has been met. There is no requirement that the DCED, the County, the Commonwealth or any other governmental entity or figure (including the Mayor or the City Solicitor) specifically consent to the chapter 9 filing. Although there may be practical constraints that result from not obtaining a prior consensus with other parties (the City’s executive officials will need to play a role in conducting a chapter 9 case, for example), the City Council retains the sole and absolute discretion to make the determination of whether to file for bankruptcy (provided that one of the requisite Act 47 authorization triggers has been satisfied).

(b) Administration of a Chapter 9 Case

(i) Role of the Judge

As compared with chapter 11 cases, the Bankruptcy Court’s power to oversee the operations of a municipal debtor is far more limited due to constitutional limitations on the federal judicial power in the context of a state body. Without the municipality’s consent, the bankruptcy court may not interfere with (1) any political or governmental power of the municipality; (2) any property or revenue of the municipality; or (3) any income-producing property of the municipality. 11 U.S.C. § 904. Accordingly, the City would not need bankruptcy court approval to use, sell or lease its property (whether in the ordinary course or outside of the ordinary course). By contrast, bankruptcy court approval is required for commercial debtors to take any action outside

of the ordinary course of business, such as selling assets. The City would not need bankruptcy court approval for any activities other than assumption or rejection of executory contracts or unexpired leases and confirmation of the Chapter 9 Plan.

Instead, the main role of the bankruptcy court is to (1) determine whether the municipality is eligible for chapter 9; (2) enforce the debtor protection provisions of chapter 9, such as the automatic stay; (3) rule on the assumption or rejection of executory contracts; (4) confirm or deny confirmation of a chapter 9 plan; and (5) dismiss or close the case, if warranted.

Because the bankruptcy court cannot order the debtor to pay or perform its obligations or otherwise impact its ability to conduct its affairs, the principal remedy the court may use to enforce compliance is dismissal of the case. A case may be dismissed for cause, including unreasonable delay by the debtor that is prejudicial to creditors, failure to propose a plan within the required time fixed by the bankruptcy court under section 941 of the Bankruptcy Code or if the court denies confirmation of a chapter 9 plan and refuses to permit the debtor to amend or to file a new chapter 9 plan. 11 U.S.C. § 930.

## (ii) Role of State Law

The Bankruptcy Code “does not limit or impair the power of a State to control, by legislation or otherwise, a municipality of or in such State in the exercise of the political or governmental powers of such municipality, including expenditures for such exercise . . . .” 11 U.S.C. § 903. “Section 903 is the constitutional mooring for Bankruptcy Code chapter 9 as it embodies a statutory declaration that enactment of municipal bankruptcy law . . . does not limit or impair the rights reserved to the States pursuant to the Tenth Amendment.” 6 Collier on Bankruptcy ¶ 903.01 (Alan N. Resnick



& Henry J. Sommer eds. 16th ed. 2010). “The purpose of this language is to remove any inference that the [chapter 9] legislation itself accomplishes anything more than providing a procedure under which municipalities may adjust their indebtedness.” Id. at ¶ 903.02[1].

Although section 903 provides that the power of a state to control a municipality in the exercise of its political or governmental powers is not limited or impaired by chapter 9, this does not allow the state to dictate which obligations can or cannot be adjusted in the chapter 9 case. In re Mission Indep. School Dist., 116 F.2d 175 (5th Cir. 1940); see In re City of Vallejo, 403 B.R. 72 (Bankr. E.D. Cal. 2009) (Bankruptcy Code authorization to reject executory collective bargaining agreement overrides state constitutional protection of such agreements). Therefore, the Commonwealth could not dictate that the City could not adjust its obligations to the County or another creditor under a confirmed chapter 9 plan.

### (iii) Automatic Stay

Upon the filing of a chapter 9 petition, an “automatic stay” is imposed against all current and future lawsuits, lien enforcement and other creditor debt collection activities. 11 U.S.C. § 362. The automatic stay stops all collection actions against the municipality and its property. Additionally, the automatic stay prevents actions against officers and inhabitants of the municipality if the action seeks to enforce a claim against the debtor. 11 U.S.C. § 922(a). “Thus, the stay prohibits a creditor from bringing or continuing a mandamus action against an officer of the municipality on account of a prepetition debt.” 6 Collier on Bankruptcy ¶ 922.02[1] (Alan N. Resnick & Henry J. Sommer eds. 16th ed. 2010). It also prohibits a creditor from bringing an action against an inhabitant of the municipality to enforce a lien on or arising out of taxes or

assessments owed to the municipality. Accordingly, the lawsuits against the City and its officers outlined above would be immediately stayed, no judgment against the City (such as for mandamus) could be enforced and no future lawsuits could be brought against the City during the pendency of the chapter 9 case (in each case, unless relief from the automatic stay were granted by the bankruptcy court).

In the absence of the automatic stay, a creditor would be free to pursue collection actions against a municipality. The creditor could bring a lawsuit (such as those that have been brought against Harrisburg), obtain a judgment and pursue enforcement proceedings that potentially could allow it to obtain a writ of mandamus and endanger the municipality's operations. Thus, the automatic stay allows the municipality to focus on its rehabilitation or reorganization, ensures that the municipality's property is not distributed outside of the bankruptcy process and prevents creditors from improving their position over other similarly situated creditors.

The filing of a chapter 9 petition does not operate to stay application of pledged special revenues to payment of indebtedness secured by such revenues (i.e., revenue bonds). Thus, an indenture trustee or other paying agent may apply pledged funds to payments coming due or distribute the pledged funds to bondholders without violating the automatic stay. See Section IV(C)(1)(c)(ii) below for more information.

(iv) Creditors' Committee

The Bankruptcy Code requires a municipality to file a list of creditors with its chapter 9 petition. Once the order for relief is entered, the United States Trustee (an official of the U.S. Department of Justice) appoints an official committee of creditors holding unsecured claims (the "Committee") to serve in the case. Typically, the Committee is comprised of the five or seven creditors holding the largest unsecured

claims. The Committee is intended to serve as a centralized body with whom the municipality can negotiate. Like all creditors in a chapter 9 case, the Committee has no direct power over the municipality and cannot create or propose a chapter 9 plan for the adjustment of the municipality's debt or force the municipality into liquidation. The Committee may retain legal and financial advisors with the approval of the Bankruptcy Court and, while the municipality is not required to pay their professional fees and expenses as it is in chapter 11 cases, municipal debtors often do so in practice in order to facilitate a consensual plan.

(v) Creditors and Claims

a. Bar Date

The bankruptcy court may fix a time within which proofs of claim<sup>88</sup> must be filed (a "bar date") in a chapter 9 case. All creditors except those whose claims are listed in the municipality's schedules as undisputed, not contingent or liquidated must file a proof of claim within the time set by the court. Any creditor who fails to do so will not be treated as a creditor with respect to the claim for purposes of voting on the plan and any recovery under the chapter 9 plan—that is, the claim will be barred. Accordingly, the establishment of a bar date aids the rehabilitation process by enabling the municipality to receive, process and analyze creditors' claims in a timely and efficient manner and to determine the universe of its potential obligations and address them with finality.

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<sup>88</sup> A "proof of claim" is a document filed with the bankruptcy court by a creditor that substantiates its claim against the bankruptcy entity. In it, the creditor asserts the amount, nature and priority of its alleged claim.

b. Role of Creditors in the Case

In general, the role of creditors in a chapter 9 case is more limited than in a chapter 11 case. For example, in a chapter 11 case, the debtor has a certain period in which to propose a chapter 9 plan, but any creditor may propose a competing plan after this exclusive period has expired. In a chapter 9 case, by contrast, only the municipality may propose a chapter 9 plan. Creditors may not ask the court to force the municipality to liquidate or to order the appointment of a trustee or other court officer to take over municipal operations or assets.

c. Treatment of Guarantors' Reimbursement Claims

Ordinarily, the Bankruptcy Code determines the validity of a claim (that is, whether the claim is "allowable") in accordance with applicable nonbankruptcy law. However, the Bankruptcy Code treats claims for reimbursement by someone who is also liable on the debtor's obligations, such as a guarantor, surety or insurer (a "co-debtor") differently than they might be treated under nonbankruptcy law. The treatment varies depending on whether the claim is (1) for an amount the co-debtor has already paid or (2) a "contingent claim"<sup>89</sup> based on the possibility that the debtor will miss payments it is required to make in the future. If the reimbursement claim is for a future payment, the claim will be disallowed in the bankruptcy, that is, the co-debtor will not share in any recovery on account of its claim. If the reimbursement claim is for a payment that the co-debtor has already made, the claim will be allowed (assuming the general requirements for allowance are satisfied). If the payment was for the entire amount

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<sup>89</sup> The definition of a "claim" in the Bankruptcy Code is extremely broad and includes a right to payment that is "contingent" on a future event happening, such as THA and the City not making a debt payment. 11 U.S.C. § 101(5).

outstanding on a particular bond issue (e.g., the County's full payment when the 2007 Notes matured), the co-debtor's reimbursement claim will be allowed in that amount and treated as a general unsecured claim against the City. However, if that payment was only a partial payment and some portion of the guaranteed debt remains outstanding, the co-debtor's claims (which are limited to the amounts of partial payments actually made) are subordinated to the remaining portion of the principal creditor's claim.

In the pending litigation against Harrisburg, the County and Assured are currently asserting claims for reimbursement of payments they made for which they are liable along with the City on some (in the case of the County) or all (in the case of Assured) of THA Facility-related debt. Thus, in a chapter 9 case, their claims will be treated under the special co-debtor rules. For the 2007 Notes, which the County has paid in full, the County would have a full reimbursement claim as a general unsecured claim. For the bonds on which the County and Assured have made only partial payments, they will have subordinated claims, which can be paid only if the bondholders' claims are satisfied in full under the Chapter 9 Plan. For the City's remaining obligations under the guaranties for future bond payments, the County and Assured will not have allowable reimbursement claims in the City's chapter 9 case, whether or not THA and the City are able to make the payments. In other words, the County's and Assured's claims in a Harrisburg bankruptcy for payments they have already made on bonds that are still outstanding stand in line behind the bondholders' claims under the Guaranty Agreements, and they have no claim in a chapter 9 case for payments they have not yet made.

The foregoing analysis is based on section 502(e)(1)(B) of the Bankruptcy Code, which provides that a claim of a co-debtor that is liable with the City (i.e., “the debtor” in bankruptcy parlance) will be disallowed to the extent that such claim for reimbursement or contribution is contingent when the court considers allowance of the claim. Because the County and Assured’s obligations to make payments on the Facility-related debt arise only when both THA and the City do not make such payments, their future rights to reimbursement (and therefore their claims in a potential chapter 9 case) are contingent, because they have not yet made those payments to the underlying bondholders and may or may not do so in the future. Therefore, under section 502(e)(1)(B) of the Bankruptcy Code, their contingent claims will be entirely disallowed in a bankruptcy case.<sup>90</sup> A claim that is disallowed does not share in any of the distributions made under the Chapter 9 Plan. However, the contingent liability would still be subject to the bankruptcy “discharge” of all prior debt that arose before the date of confirmation of the Chapter 9 Plan and, thus, following the effectiveness of a confirmed chapter 9 case of the City, the County and Assured would not have any claim against the City for any future reimbursement under the Guaranty Agreements.

The County and Assured would have allowed claims in the bankruptcy case to the extent that they have already made payments on behalf of the City on the Facility-related debt. Because the County has made \$42,092,278<sup>91</sup> in payments and

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<sup>90</sup> See Section 502(e)(1): “Notwithstanding subsections (a), (b), and (c) of this section and paragraph (2) of this subsection, the court shall disallow any claim for reimbursement or contribution of an entity that is liable with the debtor on or has secured the claim of a creditor, to the extent that . . . (B) such claim for reimbursement or contribution is contingent as of the time of allowance or disallowance of such claim for reimbursement or contribution.”

<sup>91</sup> A&M Assessment, page 51.

Assured has made \$4,039,888<sup>92</sup> in payments on the Facility-related debt, they would have allowed claims for these amounts plus the amounts of any additional payments they may make before the court determines the amount of their allowed claims. However, section 509(c) of the Bankruptcy Code would subordinate the allowed claims of the County and Assured to the remaining claims of the bondholders under the Guaranty Agreements.<sup>93</sup> Thus, the contingent claims of the bondholders for the Facility-related debt whose payment dates have not yet passed pursuant to the City's Guaranty Agreements would have priority in the bankruptcy case over the allowed claims of the County and Assured on behalf of payments they have already made pursuant to their respective guaranties and insurance on those bonds (and the claims of the County and Assured against the City in respect of future payments would be disallowed entirely).

By contrast, the claims of holders of bonds issued by other City authorities should be disallowed in a Harrisburg chapter 9 case. To date, those bonds are current, and it appears that the revenues generated by the projects or facilities that they finance will remain sufficient to pay amounts owing under the bonds. The guaranty claims under those bond issues are, like the claims under the Guaranty Agreements, contingent obligations unless and until the bond issuer fails to make a payment. Under section 502(c) of the Bankruptcy Code, the court must estimate contingent claims for purpose of allowance. Where it is likely that the contingency

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<sup>92</sup> A&M Assessment, page 51.

<sup>93</sup> Section 509(c): "The court shall subordinate to the claim of a creditor and for the benefit of such creditor an allowed claim, by way of subrogation under this section, or for reimbursement or contribution, of an entity that is liable with the debtor on, or that has secured, such creditor's claim, until such creditor's claim is paid in full, either through payments under this title or otherwise."

giving rise to the City's liability under the guarantee (i.e., nonpayment of the bonds) will not occur, a court should estimate the claim at zero, thereby disallowing the claim. Based on this analysis, the holders of guaranties on other bond issues should not have any participation in a Harrisburg chapter 9 case.

(vi) Administrative Expenses

Administrative expenses are significant because they generally must be paid in full in cash upon the debtor's emergence from bankruptcy. In contrast to chapter 11 bankruptcies which may allow administrative expenses for general operating expenses of the bankrupt entity, the only administrative expenses allowable in chapter 9 are "those incurred in connection with the chapter 9 case itself." 6 Collier on Bankruptcy ¶ 901.04[13][a] (Alan N. Resnick & Henry J. Sommer eds. 16th ed. 2010).

(vii) Contract Assumption and Rejection

One potentially significant benefit of bankruptcy is the ability to restructure contractual relationships. A chapter 9 debtor may assume favorable executory contracts<sup>94</sup> and unexpired leases and reject unfavorable ones (including collective bargaining agreements), subject to court approval. Barring a municipality's gross negligence or bad faith in exercising its discretion, the court will generally defer to the municipality's business judgment in deciding whether to assume or reject a contract or lease, allowing it wide discretion to reorganize its contractual relationships. Note that while an executory contract or unexpired lease cannot be enforced against the debtor

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<sup>94</sup> An "executory contract" is a contract under which both parties have not yet completely performed their material obligations.



prior to assumption or rejection<sup>95</sup>, the non-debtor counterparty is required to continue to perform in accordance with the terms of the contract or lease.<sup>96</sup>

a. Assumption

In general, and with limited exceptions, a municipal debtor may assume, reject or assign any executory contract, including any collective bargaining agreements, at any time before confirmation of its chapter 9 plan. 11 U.S.C. §§ 365(a), (d)(2). Assumption permits the municipality to retain the contract and its benefits after exiting bankruptcy, despite the bankruptcy filing, and prohibits the counterparty from terminating or declaring a default on the contract because of the bankruptcy<sup>97</sup> or any pre-assumption defaults. If a municipal debtor elects to assume the contract, the contract continues to bind the municipal debtor and the counterparty after bankruptcy. To assume the contract, the municipality must cure “defaults”, such as past due

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<sup>95</sup> U.S. on Behalf of Postal Service v. Dewey Freight, 31 F.3d 620 (8th Cir. 1994) (“After a debtor commences a Chapter 11 proceeding, but before executory contracts are assumed or rejected under § 365(a), those contracts remain in existence, *enforceable by the debtor but not against the debtor.*”) (italics in original); In re University Medical Center, 973 F.2d 1065, 1075 (3rd Cir. 1992) (“During [the period between filing for bankruptcy and assumption or rejection], the terms of an executory contract are temporarily unenforceable against the debtor.”).

<sup>96</sup> See Order to Compel Performance of Contract and to Enforce the Automatic Stay, In re Lehman Brothers Holding Inc., No. 08-13555 (S.D.N.Y. September 17, 2009) (Docket No. 5209) and transcript of the court’s ruling issued by Judge Peck on September 15, 2009 (available at: [http://www.google.com/url?sa=t&source=web&cd=4&ved=0CCgQFjAD&url=http://documents.epiq11.com/ViewDocument.aspx%3FDocumentPk%3De323695b-8527-43f3-a9e3-47ed2049582d&rct=j&q=case%20law%20makes%20clear%20that%20%22a%20debtor%20determines%20whether%20to%20assume%20or%20reject%20an%22%20executory%20contract,%20the%20counterparty%20to%20such%20contract%20must%20continue%20to%20perform&ei=AViLTdL4CseB0QHGs\\_jDQ&usq=AFQjCNHrwRIGJ4dYR5GaKJO35CvNB\\_k9iQ](http://www.google.com/url?sa=t&source=web&cd=4&ved=0CCgQFjAD&url=http://documents.epiq11.com/ViewDocument.aspx%3FDocumentPk%3De323695b-8527-43f3-a9e3-47ed2049582d&rct=j&q=case%20law%20makes%20clear%20that%20%22a%20debtor%20determines%20whether%20to%20assume%20or%20reject%20an%22%20executory%20contract,%20the%20counterparty%20to%20such%20contract%20must%20continue%20to%20perform&ei=AViLTdL4CseB0QHGs_jDQ&usq=AFQjCNHrwRIGJ4dYR5GaKJO35CvNB_k9iQ)) (“the case law makes clear that [until] a debtor determines whether to assume or reject an executory contract, the counterparty to such contract must continue to perform.”).

<sup>97</sup> Note that so-called “ipso facto” clauses are in almost all circumstances unenforceable. An ipso facto clause is a contractual clause that terminates or modifies (or purports to grant the non-debtor counterparty a right to do so) the contract as a result of the filing of a bankruptcy petition or the debtor’s insolvency or financial condition.

payments or other obligations that are due but unperformed, compensate the counterparty for any pecuniary loss due to breach and provide adequate assurance that the municipality will perform its future obligations under the contract. 11 U.S.C. § 365(b).<sup>98</sup> A debtor often does not assume a contract until plan confirmation to provide maximum flexibility. While a municipal debtor decides whether to assume or reject the contract, the counterparty is required to perform its obligations under the contract, and the municipal debtor must pay the counterparty for the reasonable value of any postpetition benefits received from the counterparty's continued performance.

#### b. Rejection

A rejection is a court-sanctioned breach of the contract or lease, terminating both parties' future obligations. 11 U.S.C. § 365(g). The counterparty will have a general unsecured claim for damages resulting from the breach. A debtor's threat to reject can provide significant leverage in renegotiating a contract. The ability to reject also can be a powerful tool to shed burdensome agreements and improve the municipality's cash flow. Moreover, a municipal debtor may be liable for lower damage claims upon rejection than it otherwise would be outside of the bankruptcy process because certain damage payments (such as for rejected unexpired leases) are limited by statutory formulas.<sup>99</sup>

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<sup>98</sup> These payments need not be made at the same time as the assumption, as long as adequate assurance of the payments is provided.

<sup>99</sup> For unexpired leases, a lessor's damage claim is limited by a special formula in the Bankruptcy Code as explained more fully below. The classification of such damages as general unsecured prepetition claims means that holders of such claims often receive significantly discounted recoveries.

c. Special Provisions for Unexpired Leases

The assumption, rejection or assignment of a municipal debtor's unexpired leases generally is subject to the same requirements and results in the same consequences as assumption or rejection of executory contracts, but several important provisions apply specifically to leases. As a matter of timing, a municipal debtor must assume each lease of nonresidential real property within 210 days after the court determines eligibility and orders relief or the lease will be deemed rejected.<sup>100</sup> 11 U.S.C. § 365(d)(4). If the lease is rejected, the municipality must surrender the premises to the lessor immediately. A municipal debtor must also timely perform all obligations, including rent payment, under each lease until it is either assumed, rejected or assigned. 11 U.S.C. § 365(d)(3). Each of the provisions may be waived or modified by the lessor.

The lessor of a rejected unexpired lease will have an unsecured claim for damages for breach of the lease. The lessor will be required to mitigate damages by attempting to relet the premises. However, a special Bankruptcy Code provision limits a lessor's claim for damages resulting from the termination of real property leases to the rent remaining under the lease (without acceleration), for the greater of (1) one year and (2) 15% (not to exceed three years) of the remaining lease term following the earlier of the date on which the debtor filed for bankruptcy and the date on which it surrendered the leased property plus any unpaid rent. 11 U.S.C. § 502(b)(6).

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<sup>100</sup> Harrisburg will automatically have 120 days to assume, reject or assign a lease, with up to an additional 90 days available by court order upon a showing of cause.

#### d. Collective Bargaining Agreements

Collective bargaining agreements may be modified or rejected like other executory contracts. Chapter 9 permits a municipality to unilaterally reject collective bargaining agreements without compliance with the more cumbersome procedures required in chapter 11 cases.<sup>101</sup> Accordingly, a collective bargaining agreement is easier to reject in a chapter 9 case than in a chapter 11 case. In a chapter 9 case, a court should approve rejection of a collective bargaining agreement if the municipality demonstrates that (1) the collective bargaining agreement burdens the “estate”,<sup>102</sup> (2) the equities balance in favor of rejecting the labor contract and (3) reasonable efforts to negotiate a voluntary modification have been made and are not likely to produce a prompt and satisfactory solution. NLRB v. Bildisco & Bildisco, 465 U.S. 513, 526; see In re City of Vallejo, 432 B.R. 262 (E.D. Cal. 2010) (Bildisco standards apply to review a municipal debtor’s decision to reject a collective bargaining agreement).

Moreover, under the U.S. Constitution’s Supremacy Clause, the federal bankruptcy law permitting rejection of collective bargaining agreements preempts conflicting state law. In re City of Vallejo held that a chapter 9 debtor may reject a collective bargaining agreement despite conflicting state labor law, because the federal Bankruptcy Code preempts state labor law under the Supremacy Clause. Municipalities

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<sup>101</sup> Section 1113 of the Bankruptcy Code, which imposes elaborate procedures as a condition to rejection of a collective bargaining agreement in a chapter 11 case, does not apply in a chapter 9 case. 11 U.S.C. §§ 103, 901(a).

<sup>102</sup> As a technical matter, there is no estate in a chapter 9 case. See 11 U.S.C. §§ 902(1), 904. In dicta, the Supreme Court indicated that to satisfy this standard a debtor must demonstrate that the collective bargaining agreement burdens the debtor’s ability to reorganize. Bildisco, 465 U.S. at 525-526. Accordingly, this standard has been modified in the chapter 9 context to require a showing that the agreement burdens the debtor’s ability to reorganize through the development of an effective plan of adjustment. In re City of Vallejo, 432 B.R. 262 (E.D. Cal. 2010).

must be authorized by the state in which they are located to file for bankruptcy and the California state code that authorized the municipality in the Vallejo case to utilize chapter 9 did not explicitly identify compliance with state labor law as an exception to the grant of authority for a municipality to file a chapter 9 petition. Accordingly, the court determined that “municipalities are intended to have broad authority to reject contracts and reorganize pursuant to Chapter 9, without regard to state labor laws.” Id. at 270.

Although political sensitivity surrounding the rejection process may make the prospect of rejecting the collective bargaining agreements undesirable, the threat and possibility of rejection or modification may enhance a municipal debtor’s leverage in negotiations.

(c) The Chapter 9 Plan

The chapter 9 plan is a single document that sets forth the treatment of all claims against and obligations of a municipal debtor, including executory contracts and unexpired leases, and, among other things, describes the means for the plan’s execution. It is sometimes described as a new contract between the municipality and all of its creditors, which replaces all of their individual prebankruptcy contracts with the debtor. The Chapter 9 Plan is the culmination of the debt restructuring that is supposed to occur in a chapter 9 case, and court approval (confirmation) of the chapter 9 plan is required for the municipality to leave chapter 9 successfully. A chapter 9 debtor is not subject to any statutory time limits on the filing and confirmation of a chapter 9 plan, but the bankruptcy court has the discretion to dismiss the case if the municipality delays the process unreasonably, 11 U.S.C. § 930, and most municipalities naturally seek to leave

chapter 9 as quickly as possible to escape the costs, uncertainties and burdens of the bankruptcy process.

(i) Debtor's Exclusive Right to File a Chapter 9 Plan

In a chapter 9 case, only the municipality may propose a debt adjustment plan. 11 U.S.C. § 941. Neither creditors nor the court may file alternative plans. Because creditors may not file and confirm a chapter 9 plan, the municipality preserves its full governing powers and its ability to determine how to levy taxes and make expenditures. This exclusive right has the added benefit of simplifying the bankruptcy process by eliminating the risk and distraction of multiple plans. However, as noted above, creditors may and typically do negotiate actively with the municipality over the terms of a chapter 9 plan. In addition, to comply with Act 47's requirements, Harrisburg must work with the Coordinator in developing the Chapter 9 Plan. Act 47 § 263.

(ii) Treatment of Bonds in a Chapter 9 Case

GO bonds are unsecured municipal obligations that are backed by the full faith and credit of the issuer and are payable from general tax revenues. GO bonds are treated as general unsecured debt in a chapter 9 case. We are not aware of any caselaw that holds that GO bonds' backing by the issuer's full faith and credit provide any greater priority against the issuer than other general unsecured debt. The municipality is not obligated to make payments of either principal or interest on GO bonds during the case. The obligations created by GO bonds are subject to re-negotiation and possible nonconsensual restructuring under a Chapter 9 Plan. The automatic stay of sections 362 and 922 of the Bankruptcy Code prohibits holders of GO bonds from taking any action to collect on or enforce remedies against the municipal issuer. Additionally, holders of GO bonds are not entitled to postpetition interest. 11 U.S.C. § 502(b)(2).

Revenue bonds are different and are treated differently in bankruptcy.

Revenue bonds are municipal obligations that are secured by a pledge of a stream of income described as “special revenues” by the Bankruptcy Code. 11 U.S.C. §§ 902(2), 928(a). Section 902(2) of the Bankruptcy Code provides a list of municipal income streams that qualify as “special revenues” in a chapter 9 case, including receipts from transportation and utility systems and taxes specifically levied to finance projects or systems of the municipality. The automatic stay of section 362 of the Bankruptcy Code does not operate to stay the application of pledged special revenues to payment of revenue bonds. 11 U.S.C. § 922(d). Revenue bonds continue to be secured and may be serviced during a chapter 9 case through continuing application and payment of ongoing special revenues. 11 U.S.C. § 928(a). Holders of revenue bonds can receive payment on their bonds during the chapter 9 case if special revenues are available. The bankruptcy court may not require a municipal debtor to make payments on revenue bonds, because doing so would interfere with the property or revenues of the municipality in violation of section 904 of the Bankruptcy Code.<sup>103</sup> 6 Collier on Bankruptcy ¶ 922.05[1]-[2] (Alan N. Resnick & Henry J. Sommer eds. 16th ed. 2010).

However, as a practical matter, pledged special revenues are often paid directly to the bond indenture trustee, who may apply the funds to payment of principal and interest on the revenue bonds without violating the automatic stay. In addition, section 928(a) of the Bankruptcy Code provides that “special revenues acquired by the debtor after the commencement of the case shall remain subject to any lien resulting

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<sup>103</sup> Although the Facility-related debt is primarily revenue bonds, the bonds are THA obligations, and the City’s guaranties are general obligation debt, not special revenue debt.

from any security agreement entered into by the debtor before the commencement of the case.” Accordingly, creditors holding consensual liens on special revenues of the municipality maintain their liens after the bankruptcy petition, and such revenues cannot be diverted to general uses. Section 928(a)’s “effect is to prevent special revenues that secure an issue of revenue bonds from being diverted to be available for the municipality’s general expenses or obligations.” 6 Collier on Bankruptcy ¶ 928.302 (Alan N. Resnick & Henry J. Sommer eds. 16th ed. 2010). Section 928(b) of the Bankruptcy Code limits any lien on special revenues to the net amount of revenues remaining after accounting for the necessary operating expenses of the project or system that generates the revenue.

### (iii) Classification of Claims

To describe the treatment under a chapter 9 plan of each category of claims, and to provide a means for creditors to vote on a plan, a chapter 9 plan must group claims into separate classes. 11 U.S.C. § 1123(a)(1). Claims may be placed in a class only if they are substantially similar to other claims in the same class. 11 U.S.C. § 1122(a). However, the plan may classify similar claims in separate classes if the classification of the claims is reasonable. The claims or interests in each class must be treated the same as others in that class. 11 U.S.C. § 1123(a)(4).

Classification is generally determined based on the rights that the various claim holders have against the municipality, with claims providing equal rights generally being classified together. For instance, where a debtor has two levels of secured debt, the first-lien secured claims would be in one class and the second-lien secured claims would be in a separate class. Thus, GO bonds may not be placed in the same class as revenue bonds.



Harrisburg's obligations under its guaranties of THA debt are general unsecured obligations of Harrisburg, even though the underlying THA bonds are themselves revenue bonds of THA. Accordingly, Harrisburg's obligations under its Guaranty Agreements may be classified together with Harrisburg's other general unsecured debt, such as the City's GO bonds. Because the allowed claims of the County and Assured will be subordinated under section 509 of the Bankruptcy Code, they will likely be classified separately from the claims of the indenture trustees under the City guaranties of Facility-related debt. Although unsecured creditors could all be members of one large class, it is acceptable for unsecured creditors to be divided into classes based on the treatment each type of claim is to receive under a chapter 9 plan.

(iv) Plan Requirements

The Bankruptcy Code requires that a chapter 9 plan: (1) designate classes of claims; (2) specify which classes are not impaired under the Chapter 9 Plan; (3) specify the treatment of any impaired class; (4) provide for the same treatment of each claim or interest in a particular class unless the holder agrees to a less favorable treatment; (5) provide adequate means for the Plan's implementation; and (6) not contain provisions contrary to the Bankruptcy Code.

A plan may "impair", that is, alter, the contractual, equitable or legal rights of a class of creditors and the distribution to be received by each such impaired class. 11 U.S.C. § 1123(a)(3). A class is impaired if its members' claims will not be paid in full or if the plan alters their legal, equitable or contractual rights in any way. 11 U.S.C. § 1124(1). A class that is not impaired is conclusively deemed to accept the Plan. 11 U.S.C. § 1126(f).

(v) Solicitation of Acceptances of a Chapter 9 Plan

a. Disclosure Statement

Because of the importance of the voting process, Congress has insisted that there be disclosure of adequate information, particularly of financial data, in connection with the solicitation of acceptances or rejections of a chapter 9 plan. Section 1125(b) of the Bankruptcy Code provides that “[a]n acceptance or rejection of a plan may not be solicited after the commencement of a case under this title from a holder of a claim or interest with respect to such claim or interest, unless, at the time of or before such solicitation, there is transmitted to such holder the plan or a summary of the plan, and a written disclosure statement approved, after notice and a hearing, by the court as containing adequate information.”

As a result, a chapter 9 plan must be accompanied by a “Disclosure Statement” that describes and explains it. The court rules on the adequacy of the information at a disclosure statement hearing. The relevant issue at the hearing is whether the proposed disclosure statement contains “adequate information” to enable typical holders of claims in the class to make an informed judgment about the chapter 9 plan. 11 U.S.C. § 1125(a)(1).

b. Voting and Acceptance

Voting on the plan is by class. 11 U.S.C. § 1126. An impaired class of claims has accepted a chapter 9 plan if at least two-thirds in claim amount and one-half in number of the holders of claims that actually vote in such class vote to accept. 11 U.S.C. § 1126(c). Unless the requirements for cram down, described below, are met, all impaired classes must vote to accept a Chapter 9 Plan for it to be confirmed. 11 U.S.C. § 1129(a)(8). Even if the municipality attempts to meet the cram down

requirements with respect to one or more nonaccepting classes, the court may confirm a chapter 9 plan only if at least one impaired class of claims accepts it. That is, a chapter 9 plan may not be crammed down on all classes.

(vi) Requirements for Confirmation of a Chapter 9 Plan

a. General Requirements

Section 943(b) of the Bankruptcy Code lists five general conditions required for confirmation of a chapter 9 plan:

- (1) the plan complies with the provisions of Bankruptcy Code that apply in chapter 9 cases;
- (2) the plan is proposed in good faith and not by any means forbidden by law;
- (3) the debtor is not prohibited by law from taking any action necessary to carry out the chapter 9 plan;
- (4) all amounts to be paid by the debtor or by any person for services or expenses in the case or incident to the chapter 9 plan (such as chapter 9 professional fees) have been fully disclosed and are reasonable; and
- (5) except to the extent that the holder of a particular claim has agreed to a different treatment, the plan provides that each holder of an administrative expense claim will be paid in full in cash on the effective date of the chapter 9 plan.

b. Regulatory or Electoral Approval Requirement

Section 943(b)(6) requires that any regulatory or electoral approval necessary under applicable nonbankruptcy law to carry out any provision of a chapter 9 plan has been obtained. For instance, Westfall Township's chapter 9 plan involved an increase in certain taxes, so the Township sought and obtained an order from the Pike County Court of Common Pleas under Act 47 allowing the municipality to increase tax millage for general Westfall Township purposes. Similarly, should Harrisburg desire to use the provisions of Act 47 enabling a distressed municipality to raise non-resident

earned income, real property or any other tax above otherwise applicable statutory caps, it will also have to obtain prior approval from the Dauphin County Court of Common Pleas.

c. Best Interests of Creditors and Feasible

Section 943(b)(7) requires that a Chapter 9 Plan be “in the best interests of creditors and . . . feasible.” The requirement that it be in the “best interests of creditors” means that the chapter 9 plan is “better than the alternatives that creditors have.” 6 Collier on Bankruptcy ¶ 943.03[7][a] (Alan N. Resnick & Henry J. Sommer eds. 16th ed. 2010).

In the chapter 9 context, the alternative is dismissal of the case, permitting every creditor to fend for itself in the race to obtain the mandamus remedy and to collect the proceeds. Clearly, such a result is chaos, especially in those cases where the debt burden of the municipality is too high to support on the taxes that the lands of the municipality will bear or the taxes or fees that the inhabitants or the users of municipal services will pay. Id.

Courts have applied this test in a flexible manner. “A plan that makes little or no effort to repay creditors over a reasonable period of time may not be in the best interest of creditors.” Id. Nor is a plan that requires the municipality “to devote all resources available to the repayment of creditors” as “creditors cannot expect that all excess cash go to the payment of their claims. The debtor must retain sufficient funds with which to operate and to make necessary improvements in and to maintain its facilities.” Id. Instead, “courts must find a middle ground between those extremes, and must apply the test to require a reasonable effort by the municipal debtor that is a better alternative to its creditors than dismissal of the case.” Id. On the basis of a flexible standard, “creditors can hope to receive a reasonable recovery in a chapter 9 case, and

the municipality can retain sufficient tax revenues to provide the services that inhabitants require.” Id.

The feasibility test simply requires that the municipality have the means to consummate the Chapter 9 Plan.

“In order to meet the feasibility standard, the debtor must demonstrate its ability to make the payments required under the plan and still maintain its operations at the level that it selects as necessary to the continued viability of the municipality. The court’s role will be limited to determining whether the revenue and expense projections that the debtor submits are reasonable forecasts and whether, based on those numbers, the debtor will be able to make the payments called for under the plan. As the best interest test provides a floor for payments under the plan, the feasibility test provides the ceiling, and the debtor cannot be expected to pay more than is reasonably feasible.”

6 Collier on Bankruptcy ¶ 943.03[7][b] (Alan N. Resnick & Henry J. Sommer eds. 16th ed. 2010).

d. Consenting Classes

The municipality must show that the chapter 9 plan has been accepted by each class of claims impaired under the chapter 9 plan (if a class is unimpaired, it is automatically deemed to accept the chapter 9 plan, and affirmative acceptance by that class is not required as a condition to confirmation). 11 U.S.C. § 1129(a)(8). Despite this requirement, the Bankruptcy Code grants the bankruptcy court authority to “cram down” a chapter 9 plan on a nonaccepting class of creditors (i.e., confirm it over the class’s objection) as long as (1) at least one impaired class has accepted the chapter 9 plan, (2) the chapter 9 plan “does not discriminate unfairly” against any nonaccepting class and (3) the chapter 9 plan is “fair and equitable”. 11 U.S.C. § 1129(b). Cram down can be a powerful tool to bind dissenting creditors to accept less than the face amount of their claims.

e. Cram Down

(i) Unfair Discrimination

A court may cram down a Chapter 9 Plan only if the Plan “does not discriminate unfairly” against the nonaccepting class or classes. 11 U.S.C. 1129(b)(1). Courts have determined that a plan of debt adjustment does not discriminate unfairly if a nonaccepting class is treated substantially equally to other classes of equal priority or if there is a good reason for different treatment, so that any discrimination is not “unfair”. In this context, Harrisburg’s GO bonds and its obligations under the Guaranty Agreements for the Facility-related debt and under the Covanta Guaranty Agreement are all of equal priority against the City, even though THA’s obligations under various indentures for the underlying Facility-related debt may be contractually subordinated to payment of other obligations under other indentures. By contrast, the City’s obligations to reimburse payments made by the County or Assured on Facility-related debt before the time such claims are considered for allowance in a chapter 9 case would be subordinated to other claims under section 509 of the Bankruptcy Code and therefore not have the same priority as general unsecured claims.

(ii) Fair and Equitable

A chapter 9 plan is “fair and equitable” if the chapter 9 plan provides creditors all that can be reasonably expected under the circumstances. 6 Collier on Bankruptcy ¶ 943.03[1][f] (Alan N. Resnick & Henry J. Sommer eds. 16th ed. 2010). “In determining what can be reasonably expected in the circumstances, it is not necessary for the court to take into account future inflation. A debtor’s ability to pay cannot be figured upon the condition of the district after the probable success of the plan nor after the execution of the plan nor after the advent of more fortuitous times. In determining

what can be reasonably expected under the circumstances, it is not necessary that all taxes collected go to the payment of creditors, or even that taxes be increased. The district must still have adequate revenues to continue operations, because the debtor cannot be dismantled or liquidated as in a corporate bankruptcy. Indeed, one court has held that where a debtor effectively abandons its governmental functions under a plan, the plan is not proposed in good faith.” Id. (internal quotations omitted). In Harrisburg’s case, satisfaction of the fair and equitable requirement may require, among other things, realizing value from its assets, increasing tax and fee receipts and decreasing expenditures to the maximum extent reasonable to do so.

To be “fair and equitable” to a nonaccepting class, a chapter 9 plan must also not provide any recovery to a class of claims that is subordinated or otherwise junior in priority unless all senior classes of claims have accepted the chapter 9 plan or are receiving full recovery. Thus, the subordinated reimbursement claims of the County and Assured would not be able to receive any recovery under a Harrisburg Chapter 9 Plan unless the more senior classes, such as the Facility-related debt held by the bondholders, had either accepted the Chapter 9 Plan or were being satisfied in full.

f. Discharge

Once confirmed, a chapter 9 plan is binding on the municipality, its creditors and any other party acquiring property under the chapter 9 plan. 11 U.S.C. § 944. Upon confirmation of a chapter 9 plan, the municipality receives a discharge from all debt that arose before the date of confirmation, with only two limited exceptions. These exceptions are (1) any debt excepted from discharge by the chapter 9 plan or the order confirming the chapter 9 plan and (2) any debt owed to an entity that, before confirmation of the chapter 9 plan, had neither notice nor actual knowledge of the

case. 11 U.S.C. § 944(c). In the place of its pre-bankruptcy obligations, upon its exit from bankruptcy, the municipal debtor will be subject only to any obligations specified under the confirmed chapter 9 plan.

A non-debtor entity (such as THA or the County) cannot obtain a discharge, including for liabilities for which it is jointly liable with the municipality, except in certain very limited situations. Thus, for example, discharging the City's obligations under its Guaranty Agreements would not operate to discharge THA's obligations on the Facility-related debt. Non-debtor releases are typically controversial and are often vigorously opposed. A non-debtor may obtain a release under a plan under the bankruptcy court's general equitable powers if the bankruptcy court makes specific findings that, among other things, such release is important to the reorganization and the non-debtor has provided substantial consideration to the estate in exchange for the release.

(vii) Insured Debt and its Effect

Although a confirmed Chapter 9 Plan would result in a discharge from all Harrisburg debt that arose before the date of confirmation of the Chapter 9 Plan, leaving Harrisburg with only the obligations specified under the confirmed Chapter 9 Plan, the underlying obligations of THA on its Facility-related debt, as well as any insurance or other guaranty of such debt, would be unaffected and would continue to remain outstanding to the same extent after confirmation as is currently the case. Chapter 9 would not change the maturity, interest or principal amount of the underlying debt at THA level, nor the obligations of Assured to pay to bondholders upon a default in payment by THA nor the obligations of the secondary guarantor (the County).



## (viii) Overview of the Priority Scheme

Overview of Chapter 9 Priority Scheme		
Claim	Description	As Applied to Harrisburg
<u>Administrative and priority claim</u>	Expenses of the chapter 9 case must be paid in full in cash as a condition to a chapter 9 plan confirmation.	The extent of these claims will be determined in bankruptcy.
<u>Secured claim</u>	Secured claimants are entitled to receive a distribution in cash or new or restructured debt equal to the present value of their collateral before any other creditor or interest holder is entitled to receive a distribution from the collateral.	We are not aware of any material secured claims.
<u>Revenue bond</u>	Indenture trustees may continue to apply pledged funds to payments coming due without running afoul of the automatic stay, however the bankruptcy court cannot require a municipal debtor to make payments on special revenue bonds.	Senators Revenue Bonds, Series A-1 and A-2 of 2005. If revenues of a project are insufficient to service the bonds in full, the shortfall would be treated as a general unsecured claim.
<u>Unsecured claim</u>	All unsecured claims have equal priority, unless they are expressly subordinated, and can be paid with any form of consideration (cash or restructured debt).	Examples of unsecured claims include GO bonds, the Covanta Guaranty Agreement, trade creditors, landlords and holders of tort and other litigation claims. Ordinary course of business trade and employee claims might be able to be paid in the ordinary course, without interruption.

Overview of Chapter 9 Priority Scheme		
Claim	Description	As Applied to Harrisburg
<u>Subordinated claim</u>	Creditors whose claims have been subordinated to other creditors.	The extent of these claims will be determined in bankruptcy. The allowed claims of the County and Assured for partial payments under a bond issue would be subordinated under § 509 of the Bankruptcy Code.

## 2. Interaction of Chapter 9 and Act 47

Act 47 requires that a municipality immediately notify the DCED Secretary and the Coordinator of a chapter 9 filing. Act 47 § 262. After a chapter 9 petition is filed, if the process to develop an Act 47 Plan has begun, the municipality must use the Act 47 Plan and the expertise of the Coordinator, among other tools available to it, to work out a revised Act 47 Plan to be proposed in the chapter 9 case, adapting the Act 47 Plan to incorporate bankruptcy remedies that are appropriate in the circumstances. Act 47 § 263(a). Act 47 requires that a municipality utilize the procedures set up under Act 47 concurrently with the processing of its chapter 9 case, so as to efficiently expedite the formulation of an Act 47 Plan, its timely confirmation by the bankruptcy court and its adoption by ordinance. Act 47 § 263(b). Thus, the Coordinator is still required to formulate an Act 47 Plan to be adopted by the municipality's governing body by ordinance, and the municipality will file a separate, but necessarily related, chapter 9 plan with the bankruptcy court. After adoption of an Act 47 Plan by the municipality as an ordinance and confirmation by the bankruptcy court, implementation of the Act 47 Plan must be coordinated through Act 47 and in accordance with the requirements set forth by the bankruptcy court. Act 47 § 263(c).

The procedure used in Westfall Township, which filed a chapter 9 case in 2009, may provide an instructive example. There, the Act 47 plan coordinator and Westfall Township's bankruptcy counsel worked jointly to formulate both an Act 47 recovery plan and a chapter 9 plan. On the same day, the plan coordinator filed the Act 47 recovery plan with the Westfall Township Secretary for public review, and Westfall Township's bankruptcy counsel filed a draft of the chapter 9 plan with the bankruptcy court. In accordance with Act 47, a hearing was held on the Act 47 recovery plan, and the Act 47 recovery plan was subsequently amended to reflect certain comments received from the public. This revised Act 47 recovery plan was then filed with the Westfall Township Secretary. The governing body of Westfall Township approved both the Act 47 recovery plan and the chapter 9 plan by ordinance before seeking confirmation of either plan from the bankruptcy court. A copy of the Act 47 recovery plan was attached as an exhibit to the chapter 9 plan, which was then submitted to the bankruptcy court. The chapter 9 plan included a request that the bankruptcy court confirm both plans, and the bankruptcy court did so (although it is unclear why it was necessary or appropriate for the bankruptcy court to confirm the separate Act 47 plan).

### 3. Application of Chapter 9 to Harrisburg

The filing of a chapter 9 case offers a municipal debtor protection from collection actions by creditors as well as an opportunity to adjust its debts through an established framework that includes the ability to bind all creditors (including dissenting creditors) to the chapter 9 plan and a neutral forum to resolve disputes and negotiate with creditors. If Harrisburg reaches an agreement with its creditors on a debt adjustment plan, a chapter 9 case should not be necessary, though it might be useful to

address certain technical matters in connection with the Facility-related obligation guaranties. A consensual chapter 9 case could likely be completed without a great deal of expense and time once an agreement is reached with creditors. Without creditor opposition, the bankruptcy petition could be filed along with a Chapter 9 Plan, and confirmation likely could be obtained within 60 days.

However, the dynamics and timing would change dramatically if the chapter 9 case were not consensual. The discussion below highlights some of the more important aspects of a nonconsensual chapter 9 case for Harrisburg. It focuses primarily on the debt adjustment aspects of a plan, because chapter 9 does not add appreciably to a city's ability to take other steps to restore itself to financial health, such as raising taxes or fees, improving administration or operations and disposing of or otherwise extracting value from its assets. In any event, a municipality that files for chapter 9 should have, to the greatest extent practicable, clearly formulated goals at the outset of the case as well as a well-defined exit strategy. Developing goals and an exit strategy before the filing of the case can reduce the time spent searching for solutions and expedite the process of the case.

Upon Harrisburg's filing of a nonconsensual chapter 9 case, creditors could and likely would challenge Harrisburg's eligibility to file and its "good faith" in filing. The outcome of the challenge would depend on a variety of factors, including the circumstances at the time of filing. We expect that creditors would challenge whether Harrisburg is insolvent. Because insolvency is determined based on whether a city is currently paying its debts as they become due, without regard to what steps it might take under a plan to satisfy its debts, we believe Harrisburg is insolvent as that term is defined in the Bankruptcy Code. If the City meets the pre-negotiation requirement

based on its pre-filing conduct, or if an unstayed order of mandamus is issued in any of the pending lawsuits, we believe the City should meet the eligibility and good faith requirements. Eligibility litigation could, however, delay the conduct of the case for several months. Two recent chapter 9 cases involved contested eligibility hearings that were not resolved until almost four months after the filing date.<sup>104</sup>

After the court determines eligibility, the City should continue its negotiations with creditors. However, the focus of the negotiations would likely shift. Before bankruptcy, reaching agreement with just Assured, the County and Covanta could resolve the City's Facility-related guarantee obligations. After bankruptcy, the actual bondholders would likely play a central role. As described above, an insurer or guarantor of a debtor's obligations (a "co-debtor") does not have an allowed claim in a chapter 9 case except to the extent that the co-debtor has actually paid the claim of the principal creditor, that is, the bondholders. Here, the County has paid the 2007 Notes in full, so the County's claim for reimbursement of the payments it made on the 2007 Notes (\$34.685 million) would be allowed, and the County would be allowed to participate as a full creditor for that amount. However, Assured has made only partial payments on two bond issues (about \$4 million<sup>105</sup>), and the County has made only partial payments on two other issues (about \$7.4 million<sup>106</sup>). Assured and the County would have allowed claims for the amounts that they have actually paid, but those claims would be subordinated to the claims of the bondholders, who are the principal creditors.

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<sup>104</sup> In re City of Vallejo, 2008 WL 4180008 (Bankr. E.D. Cal. 2008); In re New York City Off-Track Betting Corp., 427 B.R. 256 (Bankr. S.D.N.Y. 2010).

<sup>105</sup> A&M Assessment, page 51.

<sup>106</sup> A&M Assessment, page 51.

Thus, in a chapter 9 case, the City would be obligated to pay those claims of Assured and the County for partial payments made (about \$11.4 million as of today<sup>107</sup>, perhaps increasing during the case as Assured or the County made additional payments) only if the Chapter 9 Plan provided for the satisfaction of the bondholders' remaining claims in full. Assured and the County would likely not accept any Chapter 9 Plan that provided for such treatment, so the Chapter 9 Plan could be confirmed only under the cram down provision. The cram down provision requires that the plan be "fair and equitable" to the nonaccepting class or classes (Assured and the County), which requires the City to do all that can reasonably be expected under the circumstances to satisfy the bondholders and its other creditors. If the court confirmed a Chapter 9 Plan that paid the bondholder claims less than in full, then the City would be released from any further obligation under its reimbursement obligations to Assured and the County because the bondholder claims must be satisfied first. There is little doubt that Assured and the County would challenge this analysis and treatment of their claims, and we cannot at this early stage provide any assurance of how a court would actually rule.

During the course of the chapter 9 case, the City could also determine whether it wished to reject any of its executory contracts or unexpired leases. For example, if the City determined that it required reductions in its labor expense and had not been able to reach agreement on collective bargaining agreement modifications with its unions, then it might decide to reject one or more of the agreements and impose adjusted terms and conditions. We would expect the unions to oppose any attempt to

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<sup>107</sup> A&M Assessment, page 51.

reject collective bargaining agreements. There can be no assurance at this early stage whether a court would approve rejection nor of how City workers might react. It is possible that the court would not only approve rejection but also determine that adjustment of labor expenses is required as a condition to a cram down confirmation, because not adjusting the City's labor expenses might not be doing all that can reasonably be expected under the circumstances to enable the City to address its guarantee obligations. In other words, in determining whether to confirm a nonconsensual plan, the court will likely examine whether the proposed sacrifices are fair and equitable to nonaccepting constituencies, based on their relative rights against the City and compared to the sacrifices that other creditor constituencies are making under the plan.

A Chapter 9 Plan for Harrisburg might affect other constituencies as well. The City's GO bonds are general obligations of the City, like Harrisburg's obligations under its Guaranty Agreements and the City's guaranties of other bond issues, such as the HPA revenue bonds. However, the other guarantee claims are not likely to play a role in a chapter 9 case. A claim on a bond guarantee is allowed in a chapter 9 case based on the likelihood that the bond issuer will not be able to pay the bonds. 11 U.S.C. § 502(c). The projects or systems that the other revenue bonds have financed have not had any problems supporting the revenue bonds that the authorities have issued. Therefore, it is likely that these bondholders would either not have an allowed claim in a Harrisburg chapter 9 case or that the claim would be allowed for only a relatively small amount.

The holders of GO bonds would still have claims, and they would rank on a parity with the claims of the Facility-related bondholders under the City's Guaranty

Agreements. So, if the City's Chapter 9 Plan provided for adjustment of the amount owing on the Guaranty Agreements, it might also be required to provide for a similar adjustment on its GO bonds, if those bonds were all included in the same class under the Chapter 9 Plan. But chapter 9 permits separate classification of similar claims, such as the GO bonds and the City's obligations under its Guaranty Agreements, if the City can show a sound reason for the separate classification.<sup>108</sup> It is too early to tell whether the claims would be classified together and receive the same treatment or separately, with different treatments.

There may be numerous other, ordinary claims against the City, such as claims of suppliers of goods or services and claims of the City's employees for compensation. The City should be able to continue to pay those claims in the ordinary course of business after the bankruptcy filing, because chapter 9 does not permit the court to interfere with any of a city's property or revenues. 11 U.S.C. § 904(2). Alternatively, the City may freeze payment at the chapter 9 petition date of any such claims that were outstanding at that date to preserve cash flow and then provide for the treatment of such claims under the Chapter 9 Plan. If the City froze payment, there may be a classification issue, that is, whether those claims could be classified separately from the GO bond and Guaranty Agreement obligations and provided different treatment under the Chapter 9 Plan. Chapter 9 permits separate classification if there is a sound reason for it. The City could argue that ongoing business relations with its suppliers and labor relations with its employees require payment in full of those claims.

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<sup>108</sup> In re Jersey City Med. Center, 817 F.2d 1055 (3d Cir. 1987).



Chapter 9 permits adjustment only of the debts of the municipal debtor. It does not generally permit adjustment or release of obligations owing by a third party. Thus, Harrisburg's Chapter 9 Plan could not eliminate or modify the underlying Facility-related debt owed by THA, the guaranty obligations of the County, or the insurance obligations of Assured to the THA bondholders, all of which would remain outstanding. Chapter 9 also would not allow the City to change the principal amount, interest rate or maturity of the underlying THA-issued debt.

(a) Drawbacks of Chapter 9

Although Harrisburg could theoretically accomplish debt reduction in a chapter 9 case, it is not assured, and it could come at a substantial cost. In addition to the confirmation requirement for a cram down plan that the City do "all that can reasonably be expected under the circumstances", which might require substantial effort in raising revenue, reducing expenses and realizing value from assets, there are the direct and indirect costs of the process and the risk that a chapter 9 plan will not succeed.

(i) Expense

There are significant direct expenses attendant to a chapter 9 case, but it is difficult to estimate the final amount, because it depends on several variables. The most important variable is time, as the longer a case is pending, the higher the cost. Another variable is the degree to which other parties, particularly the Committee, contest the City's reorganization efforts. Fees for professionals such as lawyers, financial advisors and expert witnesses are likely to be substantial in a nonconsensual plan. The City of Vallejo has been involved in a hotly contested chapter 9 case for almost three years. Fees

incurred to date in that case by the City of Vallejo alone exceeded \$8.38 million as of December 31, 2010.

(ii) Time

A chapter 9 case places significant demands on the time and resources of a municipality and its officials. The chapter 9 case will almost certainly divert attention, money and other resources from Harrisburg's day-to-day operation and its efforts to return to financial health. It may prove difficult to balance the competing demands of the chapter 9 case with those of effective governance.

(iii) Right of Others to Be Heard

Chapter 9 cases generate broad public attention. In addition to creditors, representatives of the Commonwealth<sup>109</sup>, municipal employees and their unions, local residents and non-resident owners of real property, special taxpayers and others may appear and be heard in the case on some or all matters. Although their right to be heard is subject to proper courtroom procedure and such appropriate limitations as the court may impose, the multitude of parties and varying interests can cause the process to be protracted, unpredictable and subject to substantial external scrutiny.

(iv) Uncertainty

Bankruptcy is unpredictable. A judge must determine whether to confirm the City's Chapter 9 Plan and, as such, has discretion to determine whether it is reasonable. The City may not be able to obtain the requisite acceptances from creditor

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<sup>109</sup> In particular, the DCED is likely to play an active role in any chapter 9 case. The Coordinator's Act 47 Plan must be one that is "approvable by the [bankruptcy court]." Act 47 § 262(c). Section 263(a) of Act 47 requires the municipality to utilize any existing Act 47 Plan and the expertise of the Coordinator to work out a revised Act 47 Plan to be proposed in the bankruptcy court. Section 263(b) of Act 47 requires the municipality to "utilize the procedures set up by [Act 47] concurrently with the processing of" the bankruptcy case.

classes to confirm a Chapter 9 Plan consensually, to persuade the court that its Chapter 9 Plan commits the City to do “all that can reasonably be expected under the circumstances” to effect a cram down Chapter 9 Plan or be able to adjust its debts sufficiently to return the City to financial health.

(v) Adverse Effect on Credit

A bankruptcy filing could have implications for future debt issuances and on the view that rating agencies may take of the City’s prospective creditworthiness. As such, a filing could have an adverse impact on the City’s ability to raise public funds in the future or could increase its financing costs. In our experience, the magnitude of the impact on the ability to raise future capital generated by a chapter 9 filing tends to be more limited in scope and duration than is commonly anticipated.

A bankruptcy filing and its effect on the City’s perceived credit risk also may cause disruption in the City’s day-to-day operations. For instance, vendors may be reluctant to extend trade credit to a municipality in bankruptcy, at least at the outset of the case. The resulting requirement that Harrisburg deal on a cash basis would simply magnify the already burdensome strain on the City’s cash flow. The potentially adverse reputational effect that may result may also make Harrisburg appear to be a less desirable place to do business, impeding business development in Harrisburg both during and after resolution of a chapter 9 case. It might also adversely affect property values if there is uncertainty over tax rates, particularly property taxes, or the availability of city services.

Of course, many of those same effects could also result from the current uncertain state of the City’s financial situation, even in the absence of a chapter 9 filing.

## V. ALTERNATIVES AVAILABLE TO HARRISBURG

### A. Maintain Status Quo/Continuation of Default

The City could continue to default on its obligations. Outside of bankruptcy, each creditor must fend for itself and attempt to collect any unpaid debts by bringing suit or exercising any other remedies that are provided for under its contractual agreements or applicable law.

A money judgment is normally enforced by a writ of execution<sup>110</sup> unless the court directs otherwise. Fed. R. Civ. Proc. 69(a). Although this method of enforcement is appropriate for most judgment debtors, there are public policy justifications for exempting a governmental entity from the forced sale of its real or personal property to satisfy a judgment against it. Accordingly, a judgment creditor may enforce a judgment against a municipality only through an action in mandamus. A “writ of mandamus” compels the performance of a ministerial act or mandatory duty (i.e., it compels payment to the judgment creditor of the amount owed). A writ of mandamus does not permit the sale of a governmental entity’s real and personal property. If a party is able to show that a municipality has failed to pay amounts owed under a money judgment or to appropriate money for the payment of a money judgment, the court may issue a writ of mandamus directing compliance with the judgment.

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<sup>110</sup> A writ of execution is a document that is filed by a judgment creditor in a court of law and which must be approved by the court. The writ of execution serves as a lien against the debtor’s property and provides a procedure for a court officer to levy (a process by which a court officer, typically the sheriff, will obtain possession or control over a judgment debtor’s property) and sell such debtor’s real and personal property.

In the Commonwealth, such a determination is based on the Debt Act . The Debt Act was adopted to implement section 10 of Article IX of the Pennsylvania Constitution, which prescribes debt limits for municipal governments. A writ of mandamus is properly issued only where there is a clear legal right in the plaintiff, a corresponding duty in the municipal defendant, and an absence of any other appropriate and adequate remedy. The Commonwealth's Rules of Civil Procedure permit actions in mandamus to "compel performance of a public act or duty by a political subdivision of the Commonwealth . . . ." Pa. R. Civ. Proc. 1094.

Therefore, one potential consequence of continuing to default is that a plaintiff in one or more of the various lawsuits against the City and its elected officials may be successful in obtaining a writ of mandamus. The Lahr 2003 suit, for instance, seeks a writ of mandamus under § 8261 of the Debt Act if the City fails to budget, appropriate or pay the amounts due under the 2003 Guaranty Agreement in the year 2010 (which the City did not do). If the plaintiffs were successful, the court would require that the first tax moneys or other revenues received by the City be applied to the service of the applicable outstanding debt and not to payment of current general expenses. It is important to underscore the consequences of an issuance of a writ of mandamus: *all* revenue received by the City would be required to be applied toward the payment of the applicable debt. No money would be available for payment of any general operating expenses or basic City services. Such services would either cease or would have to be picked up by another party, such as the County.

We believe that if the City continues to actively engage in good faith negotiations with these plaintiffs, the plaintiffs would not seek enforcement of a writ of mandamus (even if the plaintiffs were successful in obtaining one) so long as

negotiations were continuing. This is because if the court does not stay enforcement of a writ of mandamus<sup>111</sup>, the City could prevent complete diversion of its tax revenues only by filing a chapter 9 case and obtaining the protection of the automatic stay. This “doomsday” scenario would not be in the interest of the indenture trustees under the Facility-related debt, the County or Assured as (i) the chapter 9 petition would act as an automatic stay against the mandamus action (which would be counterproductive if the plaintiffs were seeking to enforce it), (ii) they would be subject to substantial risk regarding the ultimate outcome of the bankruptcy case and (iii) the claims of the County and Assured will not be allowed in the chapter 9 case except to the extent they have already made a payment. This result should be sufficiently unattractive from the perspectives of the County and Assured that we believe they would not seek enforcement of a writ of mandamus so long as good faith negotiations with the City were ongoing.

Another consequence of continued default is that the City could impair its ability to generate future financing. Developing a track record of intentional defaults could tarnish the City’s credit reputation with credit rating agencies and the public and thus impair its ability to obtain financing or negotiate contracts with vendors and other third parties going forward.

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<sup>111</sup> The filing of the appeal will operate as a stay (or supersedeas) pending appeal against a plaintiff’s ability to obtain a mandamus order without a requirement that the political subdivision post security, subject to the right of a plaintiff to apply to the trial or appellate court for an order requiring the political subdivision to post security in order to stay enforcement of the trial court’s ruling pending appeal or to vacate the stay. See Pa. R. App. Proc. 1736-37.

## B. Financial Alternatives

### 1. Generate Funding from Certain City Assets

A municipality experiencing financial distress may consider generating funding by extracting value from its non-core assets, such as by refinancing, or a sale or lease of those assets. Management Partners published an “Emergency Financial Plan” for the City in January 2010. The Emergency Financial Plan included recommended actions to address three primary subject areas: obligations for debt service, cash management and structural financial issues. It notes that given the size of the City’s debt service obligations, asset sales or leases will likely be required to stabilize the City financially. Because no reliable information was readily available regarding the market value of various City assets, Management Partners recommended that market value appraisals be conducted for various city assets, including:

- Parking facilities;
- City Island, including all sports facilities;<sup>112</sup>
- Broad Street Market;
- Water utility and systems;
- Land under parking facilities;
- Sewerage utility and systems;

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<sup>112</sup> We believe, however, that monetization options are limited with respect to City Island. With the AA Baseball Team already sold, the City generates revenue largely from the stadium’s permit fees. These permit fees are then used to make debt service payments on the City’s revenue bonds associated with the stadium (of which approximately \$8 million in principal amount remain outstanding). However, because attendance thresholds have not been met, the City is currently subsidizing the stadium debt from its General Fund (approximately \$200,000 per year). Any transaction would need to address the stadium debt shortfalls before any funds could flow through to the City’s General Fund. Given the current economic climate, it is unlikely that City Island would generate an investment sufficiently large to provide significant relief to the General Fund. The City would also need to evaluate carefully the City Island’s deed for any legal restrictions on such a transaction.

- Resource Recovery Facility;
- City-owned museums; and
- Historic artifacts.

Asset sales and long-term leases require an extensive cost-benefit analysis, as short-term fixes to cash flow problems are unlikely to remedy the core problems afflicting Harrisburg and, in fact, may be counterproductive to procuring a sustainable solution. Indeed, the DCED Consultative Evaluation identified an unsustainable reliance on one-time revenue strategies as one of the problems contributing to Harrisburg's current financial situation.

Any transaction involving the assets of THA or the HPA must be carefully structured so that, in applying funds from the transaction to address the City's obligations, there be compliance with Pennsylvania statutes regarding the separateness of municipal authorities. Our research suggests that it will be possible to do so if existing obligations on any facility or project is refinanced, that is, if the applicable existing authority debt is repaid as part of the transaction. See MAA § 5622(a).

(a) Transactions Involving THA or its Assets

THA retained R. W. Beck to perform an appraisal study to estimate the fair market value of the Facility. R.W. Beck released its report in January 2011 (the "Facility Appraisal"). R.W. Beck estimated the value of the Facility as of January 1, 2011, considering three different approaches to valuation: (1) the Cost Approach, which considers the original cost of the Facility and estimates the cost to reproduce or replace the Facility; (2) the Income Approach, which estimates the present value of the prospective net earnings of the Facility using a discounted cash flow analysis; and (3) the Market Approach, which assess the value based on comparable sales of similar assets.



R.W. Beck concluded that the Cost Approach yielded a value of \$191,861,000, the Income Approach yielded a value of \$0 and the Market Approach was not relied upon due to an absence of suitable comparable sales. R.W. Beck concluded that, “because a potential purchaser of property should be willing to pay the lesser of the value indicated by the Replacement Cost Method (Cost Approach) and the value indicated by the Income Approach”, “the Fair Market Value at current market conditions is \$0 and that no prudent purchaser would pay any amount for the Facility, as is, without certain guarantees from [THA] *[sic]* related to minimum waste flows and minimum tipping fees.” (Section 4). R.W. Beck notes that “the Fair Market Value of the Facility is extremely sensitive to the amount of tipping fee revenue as well as the price paid for the electricity generated.”

In a separate letter, dated as of January 25, 2011, R.W. Beck employed a second discounted cash flow analysis using an “Investment Value” methodology. The “standard of value is an Investment Value representing the value of the assets to a particular owner versus the most likely purchaser. In this case the Investment Value represents the value to [THA] utilizing current operating characteristics.” (p. 1). The Investment Value analysis resulted in a value of \$159,473,000.

“While it is difficult to predict the prices a potential [private] buyer might be able to negotiate, it is apparent that the City’s contracts contain favorable rates for tipping fees, which make it reasonable to assume that value is greater to the City than to a hypothetical third-party purchaser.” (Section 4). This is because the Facility Appraisal assumes that any sale would be to a private entity and hence would be unable to receive similar tip fee rates for receiving solid waste that historically have been enjoyed by

THA.<sup>113</sup> Because a private buyer of the Facility would not be able to require residents to send their waste to the Facility and would have to charge market rates, the Facility would function at an operating loss. Accordingly, in the absence of an ability to receive similar tipping fee guaranties, R.W. Beck believes that the fair market value of the Facility upon a sale is \$0.

Since the Facility Appraisal, THA has received a proposal from the Lancaster County Solid Waste Management Authority (the “LCSWMA”) to enter into negotiations over a sale of the Facility for \$45 million.<sup>114</sup> Note that Covanta has a right of first refusal in the event that THA were to sell, lease, transfer or otherwise dispose of its rights to the Facility.<sup>115</sup> The LCSWMA proposal affirmatively stated that LCWSMA would not assume any of the outstanding Facility-related debt of THA. The proposal assumed that tipping fees would be reduced significantly<sup>116</sup>, resulting in savings for users of the Facility, but not providing value for resolution of the outstanding claims against the Facility, including the Facility-related bonds. The LCSWMA has explicitly stated that the decision to lower the City’s tipping fees “has an impact on the price established to buy the Facility.”<sup>117</sup> Accordingly, the LCSWMA may be open to

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<sup>113</sup> The Facility Appraisal assumes that municipal solid waste tip fees will be \$40 per ton for all waste received and escalate at 2.2% per year.

<sup>114</sup> The LCSWMA proposal requires \$2.1 million of the purchase price to be escrowed to pay for future tipping fees in the name of the City, at a rate of \$300,000 per year until drawn down.

<sup>115</sup> MPS, page 8.

<sup>116</sup> The proposal contemplates a reduction of tipping fees for the City from \$200 to \$78 by 2019 and a slight increase for the County over the next seven years from \$72.60 to \$78.

<sup>117</sup> [http://lcswma.org/documents/Questions\\_Answers\\_small.pdf](http://lcswma.org/documents/Questions_Answers_small.pdf).

alternative structures providing for a higher purchase price but less steep reductions of the City's tipping fees and/or increases in the County's tipping fees.

The LCSWMA proposal criticized the Facility Appraisal's "Investment Value" methodology that resulted in a value of \$159,473,000, stating that:

[u]nder this method, the consultant assumes THA would own the plant indefinitely, never have to pay any debt, and would each and every year continue to have a 'profit' of \$5,789,678 . . . indefinitely into the future. This "profit" is then discounted at 5% each year back to 2011 with the next 10 years of cash flow added to that number. Under this calculation, the [Facility] was given a value of \$159,473,000. It should be noted that to generate such a "profit", tipping fees are calculated to continue to increase at 2.2% each year to cover escalated expenses in order to maintain the annual \$5,789,678 profit level. Thus, in 2031, the City of Harrisburg tipping fee would be \$309/ton while the Dauphin County tip fee would be \$115/ton. Such a calculation is not realistic, since the tipping fees necessary to support the profit level are not sustainable or realistically affordable by either the City nor the residents and businesses in Dauphin County. Thus, the \$159 million Investment Approach valuation is not practical or applicable for an entity attempting to establish a fair valuation to acquire the Facility.<sup>118</sup>

The LCSWMA proposal contains several "contingencies" or conditions precedent to any obligation to close the transaction even after a signed agreement is executed. These include the ability of the LCSWMA to finance \$40,000,000 of the purchase price on a fully tax-exempt basis for not less than 20 years at a fixed interest rate not to exceed 6.5%, all "major operating systems" of the Facility being in "good and efficient operating condition" with an expected useful life of not less than 23 years, and confirmation that the transaction "will not involve the LCSWMA in any existing or future litigation against, by or among" THA, the City, the County or Covanta. Id.

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<sup>118</sup> <http://lcswma.org/documents/ProjectDC-ProposalComplete.pdf>.

Accordingly, the City should carefully evaluate the risks posed by a potential LCSWMA transaction as well as the potential benefits such a transaction may offer.

As an example, the R.W. Beck Analysis notes that the Facility was originally designed to sell both steam and electricity but that in March 2007, the steam line ruptured and the sale of steam was discontinued and a subsequent study by CDM dated February 11, 2008 concluded that the steam line is not safe to operate and needs replacement. (p. 11). Because the “Facility was designed such that it is capable of producing higher revenues if steam can be sold at the appropriate price” and R.W. Beck recommended that THA “should expeditiously pursue its investigations into the feasibility of resuming steam sales”, the City would want to ensure the agreement was clear as to whether the Facility’s steam components constituted a “major operating system” of the Facility (such that failure to deliver it in “good and efficient operating condition” would give the LCSWMA an option whether to close the transaction). Id.

The LCSWMA proposes to execute a memorandum of understanding by April 15, 2011, which would require all parties to “negotiate exclusively with each other concerning the transactions contemplated by [the memorandum of understanding] and not with any third parties.” Id. Because the City has expressed a desire that any asset sales or other extraordinary financial alternatives be a part of a global solution to the City’s financial problems rather than addressing only a component piece of the City’s problems, this timing may be unrealistic. Among other reasons, the Coordinator’s Act 47 Plan is not scheduled to be delivered until approximately June 1, 2011.

Alternatively, the City could seek to implement operation improvements at the Facility, increase tipping fees and improve enforcement of flow control. The R.W. Beck Analysis suggests renegotiation of the MPS with Covanta to provide greater

certainty on certain matters and increased financial incentives to Covanta to improve operations and cash flow. (R.W. Beck Analysis, pages 7-9). For instance, the current MPS places the responsibility to arrange for spot market waste and special waste on Covanta, despite the fact that there is no contractual mechanism to incentivize Covanta to maximize the tipping fee received and that Covanta's parent company operates merchant waste disposal facilities that are competitors with THA for spot market waste and special waste. (R.W. Beck Analysis, page 7-8). Additionally, the contract must be clarified to determine who bears responsibility for repairs and replacements. Currently, Covanta is claiming that such obligations are not included in their fixed fee and the costs at issue are significant. The LCSWMA proposal also highlights possible operational improvements. Facility operational improvements could increase THA's ability to contribute to debt service payments on Facility-related debt, reducing the City's guarantee burden.

Management Partners' Emergency Financial Plan contemplated a tipping fee increase as a possible deficit reducing action. (p. 25) However, we understand that City tipping fees of \$200/ton are substantially above market and that County tipping fees of about \$72/ton are also above market, although less so. This also provides an economic incentive for haulers to disregard flow control laws. Any increase in tipping fees would exacerbate the flow control enforcement issue. We are advised that THA has been addressing flow control enforcement issues more aggressively recently. In addition, THA is under a contract with the County that sets County tipping fees. A past attempt to increase them was unsuccessful. However, the County is materially at risk in the absence of a solution to the City's financial problems (because of its secondary guaranty of much of the Facility-related debt), so it should have an incentive to

contribute to an overall solution through some increase in tipping fees or otherwise, and could possibly offer greater assistance with the flow control enforcement issue.

(b) Transactions Involving the HPA or its Assets

Harrisburg's parking facilities have been identified as one of the City's most valuable assets. The HPA owns and operates 10 garages, 5 parking lots and approximately 1,200 parking meters with a combined total of 11,824 spaces located in downtown Harrisburg<sup>119</sup>, which comprises an estimated 56% of the public parking spaces in the central business district.<sup>120</sup> The HPA has seven outstanding debt obligations with a total face value of \$130,615,000<sup>121</sup> and a current principal balance owing of \$104,080,000 as of December 31, 2010.<sup>122</sup>

Several different transactions are possible with the parking assets. After a RFP process beginning in 2007 in which 50 firms were initially approached, 24 signed confidentiality agreements and three submitted proposals, the HPA selected HPP to lease the parking assets for 75 years, in exchange for an upfront payment of \$215 million and other consideration,<sup>123</sup> including capital investment in the facilities and assumption of all maintenance costs during the term of the lease. The proposal contemplated that LAZ Parking Realty Investors, LLC ("LAZ"), an experienced commercial parking

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<sup>119</sup> A&M Assessment, pages 14 and 18.

<sup>120</sup> Harrisburg Parking Authority Request for Proposals for Financial Advisory Services, dated January 28, 2011 (p. 1).

<sup>121</sup> Id.

<sup>122</sup> A&M Assessment, page 13.

<sup>123</sup> Note that because the HPA debt must also be retired, the net proceeds to the City would be around \$111 million under the 75 year structure (excluding transaction, defeasance and other costs).

operator, would operate the garages, lots and meters. We have been advised by HPP that LAZ currently operates approximately 425,000 parking spaces at 250 locations in around 28 states. For a variety of reasons, the transaction was not consummated.

We are advised that HPP remains willing to consummate the transaction largely as proposed in 2008. This type of “public private partnership” relating to parking assets has been undertaken in Chicago, Los Angeles, Pittsburgh, and Las Vegas.<sup>124</sup>

HPP has stated that it would invest \$6-8 million in the first year to install automated payment technology in garages. Under the proposal, the City would continue to collect parking taxes as a percentage of rates. The City would get 5% of the profits from the development of any air rights and the developed space would be taxable. HPP has proposed to retain all current employees with certain enhanced benefits.

The 75-year proposal could result in the realization of over \$100 million in upfront net cash proceeds, which ultimately could be applied to the outstanding Facility-related debt obligations. On the other hand, there are substantial unknown risks in a 75-year transaction.<sup>125</sup> In addition, markets generally and financing markets in particular have changed dramatically since 2008, and the City’s needs have also changed. Accordingly, the HPA may wish to consider rebidding a long-term concession contract for the parking facilities. The HPA should note, however, that there is no

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<sup>124</sup> [http://www.pittsburghlive.com/x/pittsburghtrib/news/pittsburgh/s\\_700653.html](http://www.pittsburghlive.com/x/pittsburghtrib/news/pittsburgh/s_700653.html).

<sup>125</sup> Note that HPP has also indicated a willingness to pursue a transaction for a 50-year concession for a \$195 million upfront payment.

assurance that HPP would participate or, if it did, that its offer would be on terms equal to or more favorable than those that are currently proposed. Nor is there any assurance that other bidders would be interested or would participate, as there do not appear to have been any other public expressions of interest since 2008.

Alternatively, the City might be able to attain some of the financial benefit of HPP transaction by entering into separate transactions for the parking assets. For example, hiring a commercial operator with broad experience in parking management may bring new methods and technology (such as automation) to the system and thereby increase its profitability.<sup>126</sup> A long-term contract with a commercial operator might permit the operator to finance technology upgrades to the system that would result in lower operating costs and higher yields. Of course, any such changes would have to take into account treatment of existing HPA employees. Enhanced profitability might facilitate refinancing of the HPA bonds in a higher amount, with the excess proceeds being used to reduce Facility-related obligations. Because the City can issue tax-exempt debt, it can most likely finance at a lower cost of capital than a commercial entity, such as HPP, enhancing the value that could be extracted from the parking system. Note, however, that the City cannot take advantage of the same “tax shields” from depreciation and amortization that a commercial entity, such as HPP, could utilize.

The HPA issued a Request For Proposals for general financial advisory services on January 28, 2011 and retained Boenning & Scattergood on March 24, 2011.

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<sup>126</sup> John Van Horn, editor of *Parking Today*, a trade industry publication, has stated that between 10 and 30 percent of parking revenue is typically never collected. Herb Anderson, chairman of the National Parking Association, has stated that “[b]y automating facilities, you have fewer people touching cash, and once you automate, you increase profit by making sure people pay.” [http://www.pittsburghlive.com/x/pittsburghtrib/news/pittsburgh/s\\_700653.html](http://www.pittsburghlive.com/x/pittsburghtrib/news/pittsburgh/s_700653.html).



Solicitor Tim Anderson has stated that the firm will also be available to help the HPA respond to any proposals pertaining to Harrisburg's public parking garages that come out of the City's pending Act 47 Plan.<sup>127</sup> Accordingly, the HPA has in place financial advisors should it wish to pursue this route.

The City does not directly control the HPA, so any revenue enhancements from the parking system or other transaction involving the parking system would require agreement from the HPA board.

Reliance on one-time revenue strategies without a concurrent resolution of the core problems presents material risks. But a parking asset transaction might contribute significantly to an integrated overall solution.

## 2. Renegotiate Terms of Existing Obligations

Another potential alternative is for the City to seek to renegotiate the terms of its existing obligations. The City could approach the County, Assured, vendors and other creditors to negotiate changes to its payment obligations. In doing so, the City could seek to extend the maturity date or decrease the interest rate or principal amount. Such negotiations would naturally occur in the context of the development and adoption of a plan under Act 47. However, any consensual modification to the terms of the City's debt would need to be agreed to by its creditors.

Any such renegotiation would occur in the shadow of the possibility of a chapter 9 filing by the City (as, if the City were to file for chapter 9, the filing would permit the City to suspend payment of claims). Although a creditor may (and in all

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<http://www6.lexisnexis.com/publisher/EndUser?Action=UserDisplayFullDocument&orgId=15&topicId=163690030&docId=l:1388139621&isRss=true>

likelihood would) insist on full payment, if its demands cannot reasonably be met, it risks the City's filing and obtaining court approval of a cram down plan. That process may cost the creditor in both time and expense, including legal fees, and ultimately in recovery. For even if the creditor is successful in defeating such a plan, the path to recovery may be difficult. Accordingly, the threat of a chapter 9 filing and the power a bankruptcy filing can bring to bear on a recalcitrant creditor provides useful negotiating leverage that would not be present where the possibility of a chapter 9 filing has been removed from the table.

### 3. Increase Revenues

In part because the City is the capital of the Commonwealth, only 52% of the property in the City is subject to real estate tax. (DCED Consultative Evaluation at 16). Because Harrisburg is unable to collect a significant amount of real estate tax revenue as a result, one alternative available to the City is to seek larger payments-in-lieu-of-taxes ("PILOTs") from the State and other tax-exempt entities.<sup>128</sup> PILOTs are voluntary or negotiated payments made by tax-exempt organizations to local governments, which are intended to offset the cost to the local government of providing police, fire, snow removal or other local services the tax-exempt entities receives. The PILOT amount is sometimes tied to a percentage of the amount of taxes that would be payable if the property were not tax-exempt. For instance, Lancaster's Mayor Gray has called upon Lancaster's charities for years (albeit unsuccessfully) to make PILOT

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<sup>128</sup> Note, however, that the DCED Consultative Evaluation notes (p. 16) that "[e]fforts have been made to encourage nonprofits in the City to contribute their fair share; however, the City has had very little success in gaining compliance from these tax-exempt properties. State legislation that amended the charitable organization definition has curtailed the City's efforts to obtain contributions from nonprofit charitable organizations (namely hospitals)."

payments up to 25% of what they would otherwise owe in property taxes but for their exemption.<sup>129</sup>

Nonprofits sometimes may agree to make such payments voluntarily if they have reputational incentives to contribute, as they may wish to generate goodwill in the community by contributing to local revenues. In other cases, local officials have forced the issue by threatening to levy an alternative tax on nonprofits or by challenging the entity's tax-exempt status. Often, this results in a negotiated settlement that permits the municipality to raise revenue and the nonprofit to retain community goodwill. Recent leaner economic times, especially for nonprofits, may make accomplishment of this goal more challenging.

Some PILOT payments are sponsored by governments where the state government makes direct payments to local governments based on the amount of property owned by the state or by nonprofit colleges and hospitals. Because a significant portion of the non-taxable property in the City is likely on account of its status as the capital of the Commonwealth, the City could negotiate for higher PILOT payments from the Commonwealth. It should be noted, however, that the Commonwealth already makes direct contributions to the City for fire protection for its capital buildings as well as some grants and these payments would not be reflected in the data on current Commonwealth PILOT payments.<sup>130</sup> Moreover, the Commonwealth itself is also currently suffering from budgetary constraints.

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<sup>129</sup> [http://www.pano.org/publicpolicy/publicpolicy-state\\_taxation.php](http://www.pano.org/publicpolicy/publicpolicy-state_taxation.php)

<sup>130</sup> See A&M Assessment, page 37 for additional information.

We do not have city-level data on PILOT payments to evaluate how they compare with the tax payments that would be made if those entities were not tax-exempt. It may be worth evaluating whether PILOT negotiations with the Commonwealth or the imposition of some increased payment obligation for nonprofit organizations could provide additional budget relief.

#### 4. Refunding/Refinancing of Outstanding Debt

A refinancing based on a complete resolution of the City's financial problems might result in a lower overall interest rate, reducing debt service. However, there are limitations on refunding municipal bonds and preserving tax-exempt status. These would have to be investigated carefully to ensure that the refinancing would provide the benefit of lower rates.

Harrisburg could potentially improve cash flow by refunding or advance refunding some of its outstanding debt. Generally, the purpose of a refunding is either to reduce the interest rate paid on the outstanding bonds or to remove or replace a restrictive covenant imposed by the terms of the refunded bonds. The proceeds of the refunding bonds are either deposited in escrow to pay the refunded bonds when subsequently due or applied immediately to the payment of the refunded bonds. Cash flow savings are generated by many factors including the spread between current interest rates and the interest rates of the outstanding bonds, the amount of bonds outstanding, and the time remaining before the bonds are callable. One important consideration is that federal tax law permits only one advance refunding for each debt issue so, to the extent that Harrisburg has engaged in extensive restructuring of its debt portfolio already, this option may not be available.

One source of additional value that may be available upon a refinancing is support from Assured. Under the current debt structure, either the County or Assured is obligated to make payments to holders of Facility-related debt that neither THA nor the City makes. The County or Assured will have a reimbursement claim against the City for the amounts of any such payments. Both have made clear their intention to vigorously resist, including by litigation and whether in a chapter 9 case or otherwise, any attempt to reduce the City's obligations to them on account of such payments. They would similarly oppose any City attempt to reduce the City's obligations directly to bondholders on the City's guaranties of the Facility-related debt, because reduction of the City's obligations would require the County or Assured to step in and make the payments for which the City otherwise would have been liable if THA defaults on the payments.

Assured may be willing to make a contribution to the City's restructuring efforts in various ways, as long as the City has tapped all of its reasonably available resources first. For instance, it may be willing to insure refinancing bonds, not only for the Facility-related debt, but also for other debt, including GO bond debt and, if the HPA debt is to be refinanced, for that debt as well. Insurance from a municipal bond insurer could reduce the interest rates that the City, THA or the HPA would have to pay on any new bond issue, although we are not able to determine the amount of any potential reduction. If the proceeds of the refinancing are sufficient, they could be used to repay amounts that Assured and the County have advanced on the Facility-related debt to date, holding them harmless from the prior defaults.

As a compromise with Assured, THA and the City could negotiate with Assured to insure the new debt at no cost to THA or the City, to bear the underwriting

and other issuance expenses of a refinancing, and to waive any interest on amounts already advanced. Such a compromise would allow Assured to maintain its policy position of not accepting principal reductions while permitting it to contribute to the overall solution. The County could be asked through negotiation to waive interest on the reimbursement amounts that the City and THA owe or to argue to a reduced principal amount of the reimbursement.

#### 5. Expense Reductions and Revenue Increases

The City could seek to reduce expenses through improved management of City functions and increase revenue through enhancing collection activity for taxes, fees and fines. The Coordinator's Act 47 Plan is likely to address these matters as well as other tools to help the City operate more efficiently. However, the Coordinator's analysis is not yet complete, and these matters are beyond the scope of our engagement, so we do not comment on the contribution that these actions could make to bridging the gap.

#### 6. Increasing City Taxes

A non-resident earned income tax, or commuter tax, is levied on individuals who work, but do not live, in a jurisdiction. Essentially, it is earned income tax revenue sharing between a person's hometown and their jurisdiction of employment so that commuters also contribute to where they work.<sup>131</sup>

If a municipality requests, the Court of Common Pleas can authorize a real property tax increase under an Act 47 Plan. Act 47 §§ 123 and 141. It can also

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<sup>131</sup> Note that "municipalities taxing nonresidents must credit liability for their taxes against taxes paid at the place of residence." [http://www.newpa.com/webfm\\_send/1520](http://www.newpa.com/webfm_send/1520) (p. 33).

authorize an increase in the earned income tax on non-residents. Id. A potentially important consideration is that such an action would place the burden of the increase on non-resident commuters. This may be politically unpalatable since Harrisburg is the Commonwealth's capital city and state legislators possess the power to block such an increase legislatively. Indeed, in the past, Dauphin County lawmakers have introduced legislation that would preclude the possibility of a commuter tax in Harrisburg. Such an increase also may make the City less competitive on a prospective basis relative to other jurisdictions for business location decisions. For these reasons, a financial analysis of the relative benefits and costs of any tax increase should be conducted prior to implementation.

Tax rate increases, however, do not always result in higher revenues, because higher taxes can result in increased tax defaults, in lower property values and in flight from the city, lowering total receipts. Balancing tax rates and the population's ability to pay them requires careful economic analysis that is beyond the scope of our engagement but is likely within the scope of the Coordinator's assignment. We recommend careful review of any such analysis that is included in the Coordinator's report and plan.

## VI. CONCLUSION

Whatever process the City follows to resolve its current financial difficulties, a consensual resolution, rather than a litigated chapter 9 case, would add substantial value for at least three reasons. It shortens the process. It costs less to achieve. It provides greater certainty. However, the increased value that a settlement may add must be weighed against the cost of the settlement and the cost of foregoing the possible benefit of what might be achieved in a chapter 9 case, subject to the risk of litigation.

Creditors will undertake the same sort of calculation in developing their own negotiation and litigation strategies. The possibility of a chapter 9 case and the risk that such a case may pose to creditors thus provides bargaining leverage to support the City in negotiations and to keep creditor demands at a reasonable level.

In approaching negotiations and evaluating the likelihood of possible outcomes, the City should keep in mind that the negotiation process in a financial restructuring typically is almost entirely forward-looking. It does not seek to place blame or determine who “should” bear the cost of a failure. Rather, it starts from the premise that valid obligations should be satisfied and then focuses on whether payment is feasible. To the extent that payment is feasible, the bankruptcy courts will require it.

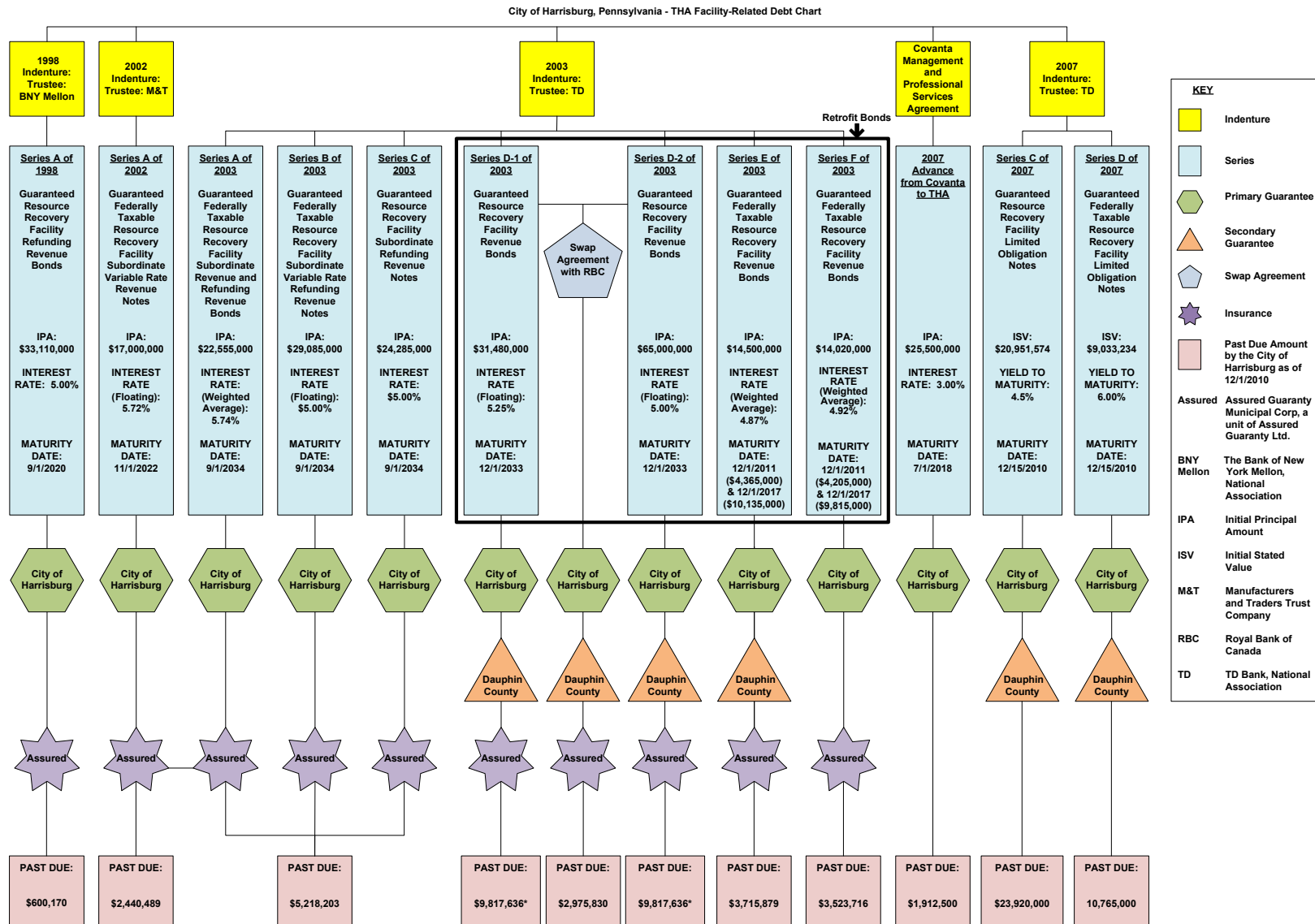


Therefore, we encourage the City of Harrisburg to evaluate carefully all sources of value and its litigation risks and negotiate a consensual resolution with its creditors. Our contacts with them suggest that they are ready to reach an agreement to resolve the City's financial problems.

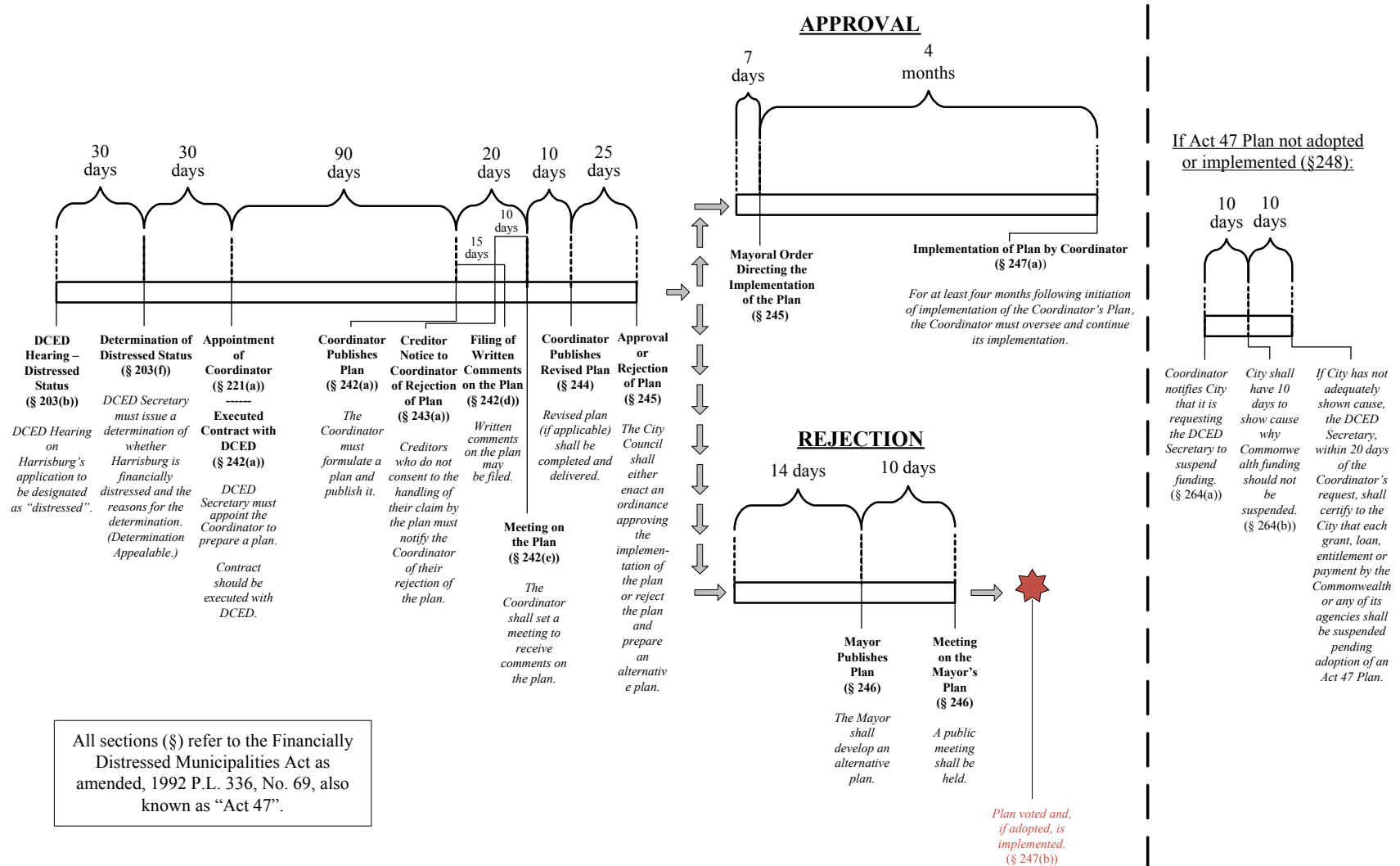
Richard Levin  
Paul H. Zumbro  
Elliott Tapp  
Campbell Agyapong

President Gloria Martin-Roberts  
Hon. Patty Kim  
Hon. Brad Koplinski  
Hon. Eugenia G. Smith  
Hon. Kelly D. Summerford  
Hon. Wanda R.D. Williams  
Hon. Susan Brown-Wilson  
c/o Beth Ann Gabler  
Office of the City Clerk  
City Government Center  
10 North Second Street, Suite 1  
Harrisburg, PA 17101

# VII. THA FACILITY-RELATED DEBT CHART



## VIII. TIMELINE OF KEY ACT 47 EVENTS

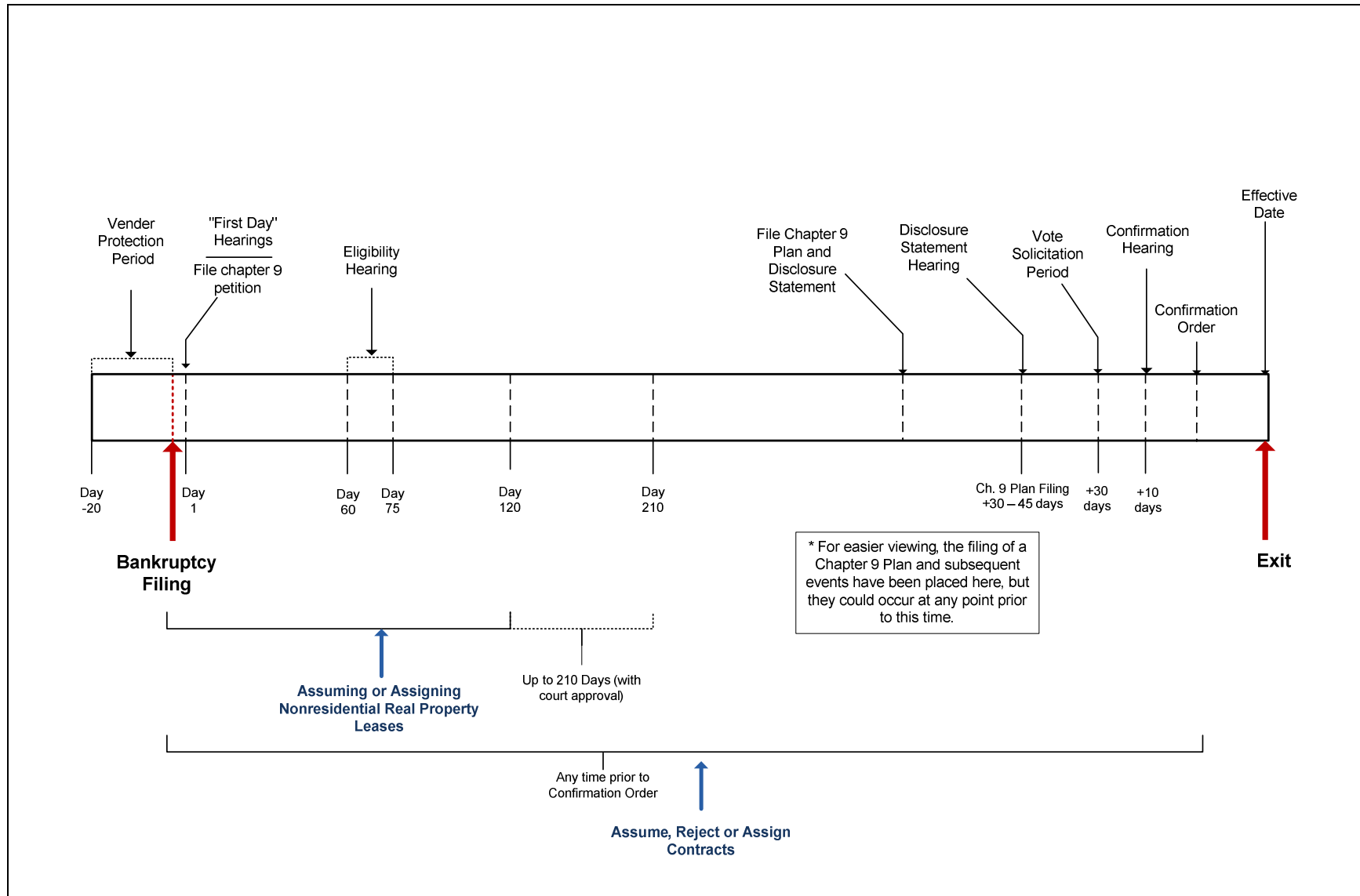


Date	Event	Description/Notes
November 17, 2010	DCED Hearing – Distressed Status (Act 47 § 203(b))	DCED held a hearing on Harrisburg’s application to be designated as “distressed”.
December 15, 2010	Determination of Distressed Status (Act 47 § 203(f))	DCED Secretary issued a determination that Harrisburg was financially distressed.
January 12, 2010	Appointment of Coordinator (Act 47 §§ 221(a) & 242(a))	DCED Secretary appointed the Coordinator. Note, however, that according to the DCED, the contract with the Coordinator has not yet been executed.
Approximately June 1, 2011	Coordinator Publishes Act 47 Plan (Act 47 § 242(a))	The Coordinator must formulate an Act 47 Plan and publish it.
Before approximately June 11, 2011	Creditor Notice to Coordinator of Rejection of Act 47 Plan (Act 47 § 243(a))	Creditors who do not consent to the handling of their claim by the Act 47 Plan must notify the Coordinator of their rejection of the Act 47 Plan no later than 10 days before the Meeting on the Act 47 Plan.
No later than approximately June 16, 2011	Filing of Written Comments on the Act 47 Plan (Act 47 § 242(d))	Written comments on the Act 47 Plan may be filed no later than 15 days after the filing of the Act 47 Plan.
Approximately June 21, 2011	Meeting on the Act 47 Plan (Act 47 § 242(e))	The Coordinator shall set a meeting to receive comments on the Act 47 Plan no later than 20 days after filing of the Act 47 Plan.
Within 10 days of the Meeting on the Act 47 Plan	Coordinator Publishes Revised Act 47 Plan (Act 47 § 244)	Revised Act 47 Plan (if applicable) shall be completed and delivered.
Within 25 days of the Meeting on the Act 47 Plan	Approval or Rejection of Act 47 Plan (Act 47 § 245)	The City Council shall either enact an ordinance approving the implementation of the Act 47 Plan or reject the Act 47 Plan and prepare an alternative Act 47 Plan.
Within 7 days of Approval of Act 47 Plan	Mayoral Order Directing the Implementation of the Act 47 Plan (Act 47 § 245)	The Mayor enters an order directing implementation of the Act 47 Plan.
[Within 14 days of any rejection of the Coordinator’s Act 47 Plan ] <sup>132</sup>	[Mayor Publishes Act 47 Plan (Act 47 § 246)]	[If applicable, the Mayor shall develop an alternative Act 47 Plan.]
[Within 10 days of publishing of the Mayor’s Act 47 Plan ]	[Meeting on the Mayor’s Act 47 Plan (Act 47 § 246)]	[If applicable, a public meeting shall be held on the Mayor’s alternative Act 47 Plan.]

<sup>132</sup> Note that items are bracketed if they are contingent on the occurrence of a particular event and will not necessarily occur under the Act 47 process.

Date	Event	Description/Notes
Until 4 months after Act 47 Plan Implementation	Implementation of Act 47 Plan by Coordinator (Act 47 § 247(a))	For at least four months following initiation of implementation of the Coordinator's Act 47 Plan, the Coordinator must oversee and continue its implementation.
[Upon failure to adopt or implement an Act 47 Plan]	[Coordinator Notification to City. (Act 47 § 248)]	[The Coordinator must notify the City that he is requesting the DCED Secretary to suspend Commonwealth funding to the municipality. ]
[Within 10 days of failure to adopt or implement an Act 47 Plan]	[City must show cause to the DCED Secretary and Coordinator why funding should not be suspended. (Act 47 § 264(a))]	[The City shall have 10 days from the date of the Coordinator's notice in which to show cause to the DCED Secretary and the Coordinator why Commonwealth funding to the City should not be suspended.]
[Within 20 days of the Coordinator's request]	[DCED Secretary certifies to City that Commonwealth funding shall be suspended]	[If the City has not adequately shown cause to the DCED Secretary and the Coordinator why such funding should not be suspended, the DCED Secretary, within 20 days of the Coordinator's request, shall certify to the City in writing that each grant, loan entitlement or payment by the Commonwealth or any of its agencies shall be suspended pending adoption of an Act 47 Plan calculated to fully resolve the City's financial distress.]

## IX. TIMELINE OF KEY BANKRUPTCY EVENTS



Date	Event	Description/Notes
-20 days	Vendor Protection Period	All claims of vendors for the value of any goods sold to a municipality in the ordinary course and received within 20 days prior to filing must be paid in full on or before confirmation.
<b>Bankruptcy Filing</b>		
1 day	File chapter 9 petition (the " <u>Petition Date</u> ")	Typically, a chapter 9 debtor files a list of creditors with its voluntary petition. Section 923 requires publication of a notice of commencement of the case and of a notice of an order for relief. Notices must be published at least once a week for three successive weeks in at least one newspaper of general circulation within the district of filing, and at least one other publication with general circulation among bond dealers and bondholders as the court designates. The initial notice must include the date by which creditors and parties in interest must file any objections to eligibility.
1 day	"First Day" Hearings	At the beginning of the bankruptcy case, the court will approve the notice of commencement and set a schedule for any objections to the chapter 9 petition under section 921 of the Bankruptcy Code.
60-75 days	Eligibility Hearing	Between 60-75 days after the filing of the petition, the court will hold a hearing on any objections to the chapter 9 petition that have been filed.
120 days	Deadline for Assuming or Assigning Nonresidential Real Property Leases	Nonresidential real property leases are deemed rejected if not assumed within 120 days after the court determines eligibility and orders relief (extendable up to 210 days).
210 days (Maximum)	Deadline for Assuming or Assigning Nonresidential Real Property Leases	Nonresidential real property leases are deemed rejected if not assumed within a maximum of 210 days after the court determines eligibility and orders relief (with court approved extension).
Any time prior to Confirmation Order	Assume, Reject or Assign Contracts	The municipality may assume, reject or assign executory contracts and personal property leases at any time prior to confirmation of the Chapter 9 Plan.
Any time after Petition Date	File Chapter 9 Plan and Disclosure Statement	The municipality must file a Chapter 9 Plan and Disclosure Statement.
30-45 days after filing of Chapter 9 Plan and Disclosure Statement	Disclosure Statement Hearing	The court holds a hearing to approve the Disclosure Statement.
Approximately 30 Days after Disclosure Statement Hearing	Vote Solicitation Period	The municipality may solicit votes on its Chapter 9 Plan from creditors.

Date	Event	Description/Notes
Approximately 10 Days after conclusion of Vote Solicitation Period	Confirmation Hearing and Confirmation Order	The court holds a hearing on whether to confirm the Chapter 9 Plan. After the Confirmation Order and before the Effective Date, the City must obtain any required regulatory, electoral, legislative or judicial approvals necessary to implement the Chapter 9 Plan.
After Confirmation Order	Effective Date	On the Effective Date, the automatic stay is lifted, the Chapter 9 Plan becomes binding and the discharge of all prior debt becomes effective.



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# The City of Harrisburg

## Restructuring Alternatives Assessment

LEADERSHIP • PROBLEM SOLVING • VALUE CREATION



March 30th, 2011



ALVAREZ & MARSAL

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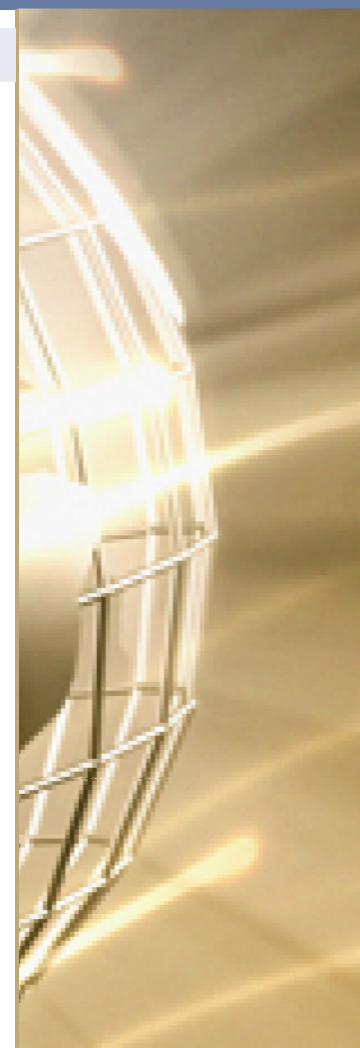
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# I. Background

The City of Harrisburg, PA is currently in the midst of a debt crisis and needs to de-lever its balance sheet

**The City guarantees \$242 million of debt issued by The Harrisburg Authority (“THA”), the majority to refurbish its waste-to-energy incinerator (“Resource Recovery Facility” or “RRF”) which lacks the revenue to meet its debt obligations.**

- ▲ To date, THA/RRF has missed \$65 million in principal and interest payments, which have been covered by either the County, Assured Guaranty Municipal Corporation (“AGM”) or the Debt Service Reserve Funds (“DSRF”).

**Bankruptcy has been mentioned in the media, however a proceeding should only be undertaken as a measure of last resort.**

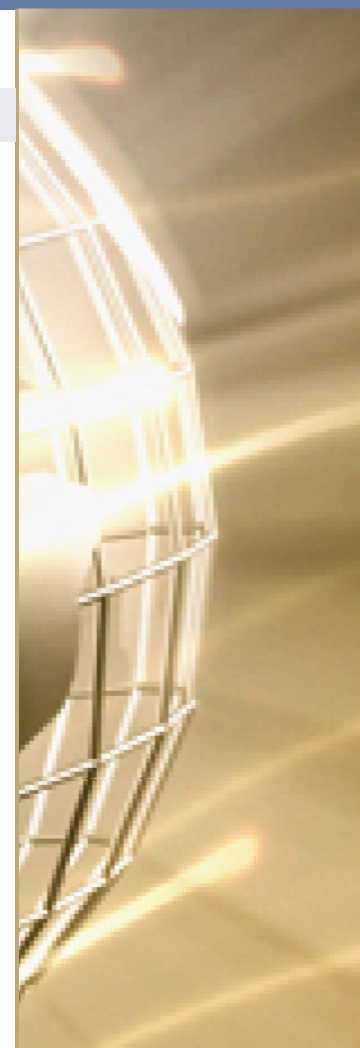
- ▲ Despite advantageous debtor powers under chapter 9, a chapter 9 plan would likely revolve around a combination of fiscal improvements and monetization of assets, which are also available out of court.

**To address the inability of the City to meet guarantee obligations and reduce debt service going forward, most involved parties seem to believe that asset monetizations (such as sale or capital leases) are the best route to allow major principal pay downs and a restructuring of remaining debt.**

- ▲ Although most news stories have focused on the Harrisburg Parking Authority (“HPA”), which has already received an offer of \$195-\$215 million, monetization of other public assets including the RRF and debt refinancing may also contribute to balancing the budget.

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## II. City Financial Position

The Act 47 Coordinator's projection of the City's 2011 Budget reflects a deficit of \$3.0 million, even before THA guaranteed debt obligations

City Budget Summary <sup>1</sup>				
(\$s in Millions)	2010 Actual	2011 Projected	Variance Fav/(Unfav)	
<u>Revenues:</u>				
General Fund Revenue	\$ 37.40	\$ 44.51	\$ 7.10	
Water Fund Revenue	16.08	18.19	2.11	
Sewer Fund Revenue	13.73	14.62	0.89	
Sanitation Fund Revenue	4.12	4.47	0.35	
State Liquid Fuels Fund Revenue	0.89	0.89	(0.00)	
Other Revenue / Asset Sales	0.51	1.01	0.50	
<b>Total City Revenue</b>	<b>72.74</b>	<b>83.70</b>	<b>10.96</b>	
<u>Operating Expenses:</u>				
General Fund	40.63	44.79	(4.15)	
Water Fund	3.36	4.02	(0.66)	
Sewer Fund	4.87	7.40	(2.53)	
Sanitation Fund	1.48	1.76	(0.28)	
State Liquid Fuels Fund	0.75	0.89	(0.15)	
<b>Total City Operating Expenses</b>	<b>51.08</b>	<b>58.85</b>	<b>(7.78)</b>	
<b>Operating Surplus</b>	<b>\$ 21.66</b>	<b>\$ 24.84</b>	<b>\$ 3.18</b>	
<u>Non-Operating Expenses:</u>				
Cap Ex	0.28	0.40	(0.12)	
Debt Service (General Fund)	11.50	12.22	(0.72)	
Debt Service (Water Fund)	13.18	10.88	2.29	
Debt Service (Sewer Fund)	2.05	2.16	(0.11)	
Non-Operating Expenses	27.01	25.66	1.35	
<b>Act 47 Adjustment<sup>2</sup></b>		<b>(2.18)</b>	<b>(2.18)</b>	
<b>Surplus / Deficit<sup>2</sup></b>	<b>\$ (5.35)</b>	<b>\$ (3.00)</b>	<b>\$ 2.35</b>	

Sources: a. Data from City Controller's Office; b. Water Fund Budget (THA)

Notes: 1. See Appendix - City Interfund Detail for further information

2. The Act 47 Coordinator has run a detailed forecast of the 2011 City budget and projects a deficit of approximately \$3.0 million



## II. City Financial Position

The City guarantees \$242 million of debt at THA/RRF – to be current by FYE 2011, the City will need to cover a combined \$83 million of past due payments and 2011 debt service

THA/RRF Debt (as of 12/31/2010)																		
(in Millions)		A	B	C					D = A+B+C	E	F = E+C							
		2011	2011	Past Due Owed by City					2011	Total Principal	Total Principal							
		Principal	Interest						Debt Service	Outstanding	at 1/1/2011							
		Due	Due	DSRF <sup>1</sup>	County	AGM	Total	and Past Due	at 1/1/2011 <sup>2</sup>	and Past Due								
<u>County Guaranteed/AGM Insured:</u>																		
Revenue Bonds, Series D of 2003	\$	-	\$	6.40	\$	8.00	\$	4.79	\$	-	\$	12.79	\$	19.19	\$	96.48	\$	109.27
Revenue Bonds, Series E of 2003		1.52		0.58		1.10		2.62		-		3.72		5.82		11.66		15.37
Notes, Series C of 2007		-		-		-		23.92		-		23.92		23.92		-		23.92
Notes, Series D of 2007		-		-		-		10.77		-		10.77		10.77		-		10.77
County Guaranteed/AGM Insured		1.52		6.98		9.10		42.09		-		51.19		59.69		108.14		159.33
<u>AGM Insured</u>																		
Revenue Bonds, Series A of 1998		-		0.56		0.60		-		-		0.60		1.16		11.17		11.77
Notes, Series A of 2003		0.84		0.81		0.80		-		1.64		2.44		4.09		14.08		16.52
Revenue Bonds, Series A, B, C of 2003		-		3.32		5.22		-		-		5.22		8.53		75.93		81.14
Revenue Bonds, Series F of 2003		1.47		0.57		1.12		-		2.40		3.52		5.56		11.28		14.80
Total AGM Insured		2.31		5.25		7.74		-		4.04		11.78		19.33		112.45		124.23
Covanta Loan (City Backed)		1.89		0.15		-		-		-		1.91		3.95		21.04		22.95
<u>Total THA/RRF Debt Service</u>																		
	\$	3.71	\$	12.37	\$	16.84	\$	42.09	\$	4.04	\$	64.89	\$	82.97	\$	241.62	\$	306.51

Sources: a. Data from City Controller's Office; b. Indentured Trustee Data

Notes: 1. The City is obligated to replenish the DSRF to remain current on the existing notes and bonds

2. Consists of principal due in 2011 and all principal due from 1/1/2012 onward for each issue

## II. City Financial Position

Because of limited available cash and a projected Budget deficit, the City faces a \$14 million shortfall in 2011 after THA/RRF debt service and a \$79 million shortfall after the repayment of past due amounts

Shortfall from THA/RRF Guarantees	
(\$s in Millions)	2011 Projected
Cash as of March 17, 2011 <sup>1</sup>	\$ 7.05
2011 Budget Deficit before THA/RRF Guarantees	(3.00)
<b>Cash to Service THA/RRF Obligations</b>	<b>\$ 4.05</b>
2011 THA/RRF 2011 Debt Service	
2011 Interest	\$ 12.37
2011 Principal	5.71
Total 2011 THA/RRF Debt Service	18.09
<b>Cash Shortfall to Service 2011 THA/RRF Payments</b>	<b>\$ (14.04)</b>
THA/RRF Debt Past Due Payments	
Missed Payments (County)	\$ 42.09
Missed Payments (Assured)	4.04
Missed Payments (DSRF Replenishment) <sup>2</sup>	16.84
Covanta Loan	1.91
Total THA/RRF Debt Past Due Payments	64.89
<b>2011 Cash Shortfall to Service All THA/RRF Obligations</b>	<b>\$ (78.93)</b>

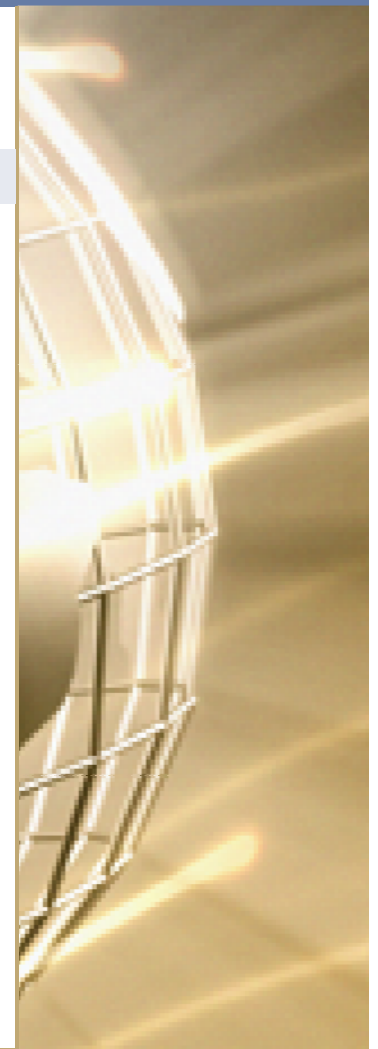
Sources: a. Data from City Controller's Office; b. Water Fund Budget (THA)

Notes: 1. See Appendix - City Cash Position

2. The City is obligated to replenish the DSRF to remain current on existing Notes

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### III. Alternatives – Chapter 9

The City may seek protection under chapter 9 of the Bankruptcy Code

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**Chapter 9 provides a financially distressed “municipality” protection from its creditors while it develops and negotiates a plan for adjusting its debts.**

**Only municipalities defined as a “political subdivision or public agency or instrumentality of a state” are eligible and must satisfy four threshold requirements to obtain relief:**

- ▲ Have specific State authorization to be a debtor under chapter 9
- ▲ Be Insolvent (Not paying current obligations as they become due)
- ▲ Desire to effect a plan to adjust its debt
- ▲ Satisfy one of the following four conditions:
  - Has obtained the consent of at least a majority in amount of impaired claimholders under a proposed plan
  - Has negotiated in good faith but has failed to reach agreement with a majority of impaired claimholders under a proposed plan
  - Negotiation with such claimholders is impracticable
  - Has a reasonable belief that a creditor may attempt to obtain a preference

### III. Alternatives – Chapter 9

Under a chapter 9 case, the City is obligated to do all that can reasonably be expected to satisfy creditors' claims

---

#### **Chapter 9, in general, provides for the following protections:**

- ▲ Automatic stay of any creditor collection action.
- ▲ Assume or reject executory contracts.
- ▲ Section 1113 of the Bankruptcy Code contains stringent requirements that must be met before the debtor may reject a union contract. This provision is not part of the chapter 9 process. Accordingly, a chapter 9 municipality may reject collective bargaining agreements without compliance with the more cumbersome procedures required in chapter 11.
- ▲ Only the City may propose a debt adjustment plan.
- ▲ Liquidation of assets is not available to creditors - their choice is to accept or reject the debtor's plan or, if the case is dismissed, pursue individual remedies, including litigation.

#### **“Best Interests of the Creditors” test:**

- ▲ Chapter 9 permits a city to gain bankruptcy court approval of a plan over the objections of dissenting creditors only if certain statutory conditions are met.
- ▲ Attempting to confirm a nonconsensual plan under this condition is likely to involve extensive litigation.

### III. Alternatives – Out of Court Restructuring

Political risks and excess costs can be defrayed by avoiding bankruptcy

Despite advantageous debtor powers under chapter 9, a chapter 9 plan of debt adjustment would likely involve some combination of operational improvements, budget adjustments, revenue enhancements, expenditure reductions, including from contract renegotiations, asset sales, debt refinancings and debt reductions or other adjustments, which are also available out of court.

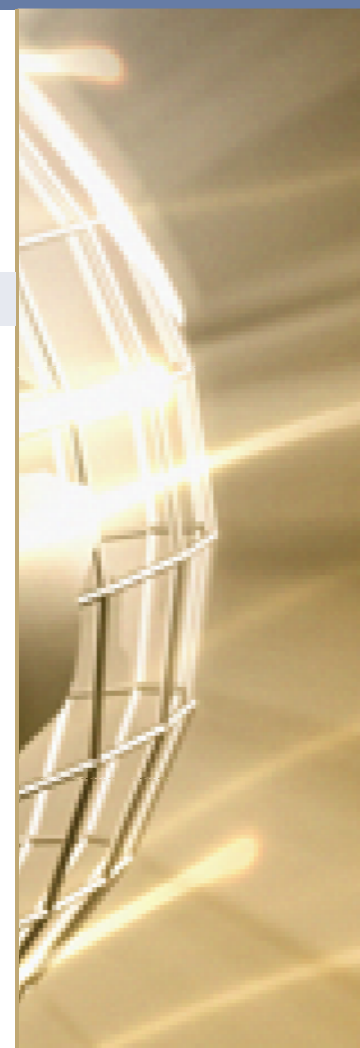
#### Benefits of avoiding bankruptcy include:

- ▲ Defrayment of expenses of a court proceeding and potential future litigations
- ▲ Avoidance of the public stigma of bankruptcy
- ▲ Should a consensual out of court plan be adopted, ability to refinance may be improved (improved credit status for city, county and state)

To execute an out of court solution, the City will need to negotiate and consensually reach a plan of debt adjustment supported by its creditors while pursuing fiscal improvements and the monetization of assets.

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## IV. Monetization Options – Harrisburg Parking Authority

The Harrisburg Parking Authority (“HPA”) is seen by many as having the best monetization potential for the City

### HPA Background:

- ▲ As a state capital city, Harrisburg has significant commuter traffic, and consequently, has a large parking system in relation to its residential population.
- ▲ The HPA currently provides approximately \$4 million in cash to the City each year (including approximately \$1.9 million in parking taxes).
- ▲ Capital expenditures are needed to modernize and improve current facilities.
  - Major repairs and projects are funded by bond issuances – current debt balance is \$104.1 million
  - Any improvements will need to be funded by additional debt

### Potential Alternatives:

- ▲ Automation: Parking System is currently on a cash only basis and cash controls may not be adequate. An automated credit/debit card pay-system may increase revenues, however, updating the system is estimated to cost \$5 to \$10 million (per HPP offer).
- ▲ Private Operator: Operating efficiency and cash controls may be improved by involving a private entity to manage operations. Economics of an operating agreement still need to be explored and would likely need to be done in conjunction with automating the system.
- ▲ Concession/Long-term Lease: Long-term concession of the parking system would provide a significant upfront payment and require giving up virtually all control of the parking system to the concessionaire.
  - City would still set parking meter rates, parking taxes and violation fines
  - Concessionaire would have rights to all revenues and would be responsible for all costs, including capital expenditures



## IV. Monetization Options – Harrisburg Parking Authority

Harrisburg's parking assets consist of 10 garages with 7,952 spaces and 5 lots with 2,672 spaces (including handicap) in addition to approximately 1,200 metered spaces

Parking Facility	Address	Type	Standard Spaces	Handicap Spaces	Total Spaces
Chestnut Street	322-326 Chestnut Street	Garage	1,000	21	1,021
Walnut Street	215 Walnut Street	Garage	1,032	20	1052
5th Street	6-14 North 5th Street	Garage	856	17	873
River Street	218 North 2nd Street	Garage	850	17	867
South Street	220 South Street	Garage	736	16	752
Locust Street	214 Locust Street	Garage	628	13	641
Market Square	34 South 2nd Street	Garage	577	12	589
City Island	Market Street Bridge	Garage	484	0	484
7th Street	801-813 North 7th Street	Garage	1,182	15	1197
Harrisburg University	326 Market Street	Garage	380	8	388
			<b>7,813</b>	<b>139</b>	<b>7,952</b>
City Island North	Market Street Bridge	Lot	1,395	11	1406
City Island South	Market Street Bridge	Lot	847	39	886
7th Street	801-813 North 7th Street	Lot	152	15	167
10th & Mulberry	10th & Mulberry Street	Lot	128	0	128
Mulberry Street	3rd & Mulberry	Lot	85	0	85
			<b>2,607</b>	<b>65</b>	<b>2,672</b>
Metered Parking	Throughout Municipality	Meters	> 1,200	0	> 1,200

## IV. Monetization Options – Harrisburg Parking Authority

The concession of the City's parking system may have the greatest potential to provide a significant one-time liquidity infusion / debt reduction

**Note:** The bid discussed hereafter was received through a process conducted several years ago and is presented solely to illustrate a potential lease structure and does not constitute an endorsement or recommendation. Should the City ultimately decide to pursue a concession, it should consider whether to undertake a renewed competitive bid process.

In 2007, the HPA and Royal Bank of Canada (“RBC”) conducted a competitive bid process on behalf of the City to lease the parking system.

- ▲ 50 potential concessionaires solicited
- ▲ Harrisburg Public Parking, LLC (“HPP”) selected as highest and best bid, however, the transaction was never consummated

**HPP has re-approached the city and made the following offer:**

- ▲ 75-year concession: \$215 million upfront payment
- ▲ 50-year concession: \$195 million upfront payment

**After defeasance of the HPA debt, proceeds will be available to reduce some of THA bond obligations.**

Proceeds to Reduce THA/RRF Obligations			
<i>(\$s in Millions)</i>		50-Year Projected	75-Year Projected
Upfront Payment	\$	195.00	\$ 215.00
Defeasance of HPA Debt <sup>1</sup>		(104.08)	(104.08)
<b>Net Proceeds to the City</b>	<b>\$</b>	<b>90.92</b>	<b>\$ 110.92</b>

Notes: 1. Excludes transaction, refinancing, and defeasance costs

## IV. Monetization Options – Harrisburg Parking Authority

While the upfront payment can be used to defease or to reduce debt obligations of both the HPA and THA, the City will forego proceeds otherwise available from HPA operations for the duration of the concession

### Annual Lost Proceeds to City

(\$s in Millions)

Estimated  
Annual Loss

#### HPA Profit Sharing:

2011 HPA Transfer to City	\$	4.00
2011 Estimate Parking Taxes		(1.88)
2009 Investment Income		(0.30)
<b>Net Contribution to City</b>		<b>1.82</b>

#### Additional Considerations:

2010 Parking Fines		1.11
2010 Enforcement Costs		(0.39)
HPP Profit Sharing		(0.25)
<b>Parking Enforcement to City</b>		<b>0.47</b>

**Estimated Annual Foregone Proceeds to City<sup>1</sup> \$ 2.29**

Source: Data from City Controller's Office, 2010-2011 budget

Notes: 1. May be greater should HPA Operations/Profitability be improved

## IV. Monetization Options – Harrisburg Parking Authority

Given its timing and location, the Pittsburgh Parking Authority's 50-year lease of its parking assets for \$452MM presents a valuable comparison for the HPA

	Harrisburg Parking Authority	Pittsburgh Parking Authority	Chicago On-Street Parking (Metered Parking)	Pennsylvania Turnpike	Chicago Off-Street Parking (Garage Parking)	Indiana Toll Road	Chicago Skyway
Date	Current HPP Offer(s)	September 2010	December 2008	May 2008	December 2006	June 2006	January 2005
Value (\$ in MM)	\$215 / \$195	\$452	\$1,157	\$12,800	\$563	\$3,800	\$1,830
Term	75 years / 50 years	50 years	75 years	75 years	99 years	75 years	99 years
Key Metrics	-7,952 spaces in 10 garages -2,672 spaces in 5 lots -Approximately 1,200 parking meters	-8,946 spaces in 12 Garages -1,776 off-street meters in 33 surface lots -6,931 on-street meters	- Approximately 36,000 spaces	- East-West Mainline (I-276/I-76/I-70), Northeast Extension (I-476), Western Expansions (excluding Mon-Fayette Expressway/Southern Beltway) and related administrative and maintenance buildings	- 9,176 spaces in 4 Garages	- 2-3 lanes in each direction, 157 mile toll road running the length of northern Indiana, which averages approximately 130,000 transactions per day	- 6-lane (3 in each direction), 7.8 mile long toll road providing access from northern Indiana to downtown Chicago

## IV. Monetization Options – Harrisburg Parking Authority

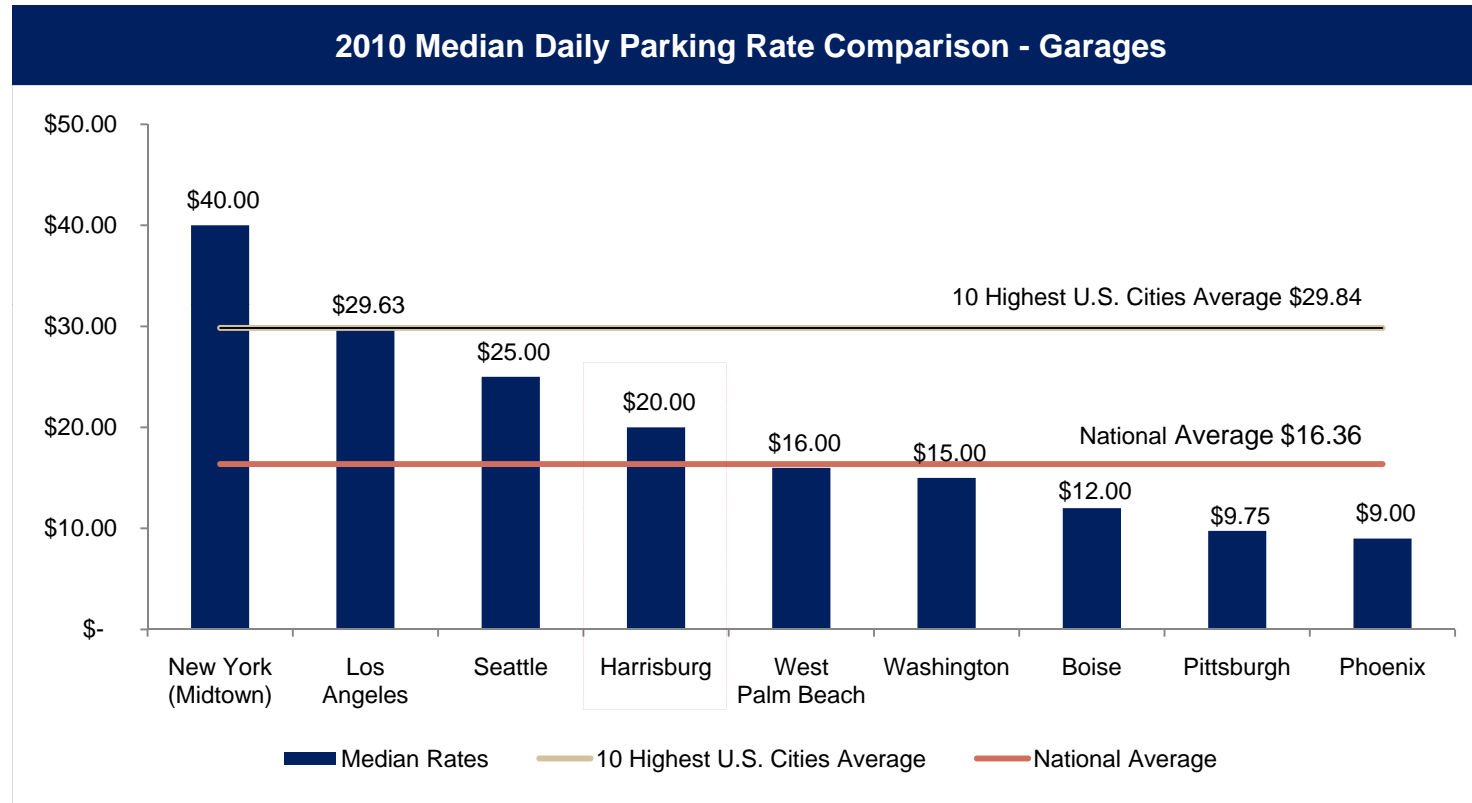
Pittsburgh's inventory of parking assets is significantly higher than Harrisburg's in terms of the total number of parking spaces across the various channels

	Garages		Lots		Metered Parking	Total Garages, Lots	Offers Received	
	# of Locations	# of Spaces	# of Locations	# of Spaces	# of Spaces	# of Spaces	50-Year Lease (\$s in Millions)	\$/Space
Harrisburg Parking Authority	10	7,952	5	2,672	> 1,200	11,824	\$195	\$16,492
Pittsburgh Parking Authority	12	8,946	33	1,776	6,931	17,653	\$452	\$25,605

The HPP's 50-Year offer for the HPA represents an approximately \$16,500 value per space. This is 55% lower as compared to the Pittsburgh concession of \$25,605 value per space.

## IV. Harrisburg Parking Authority Median Daily Parking Rate Comparison

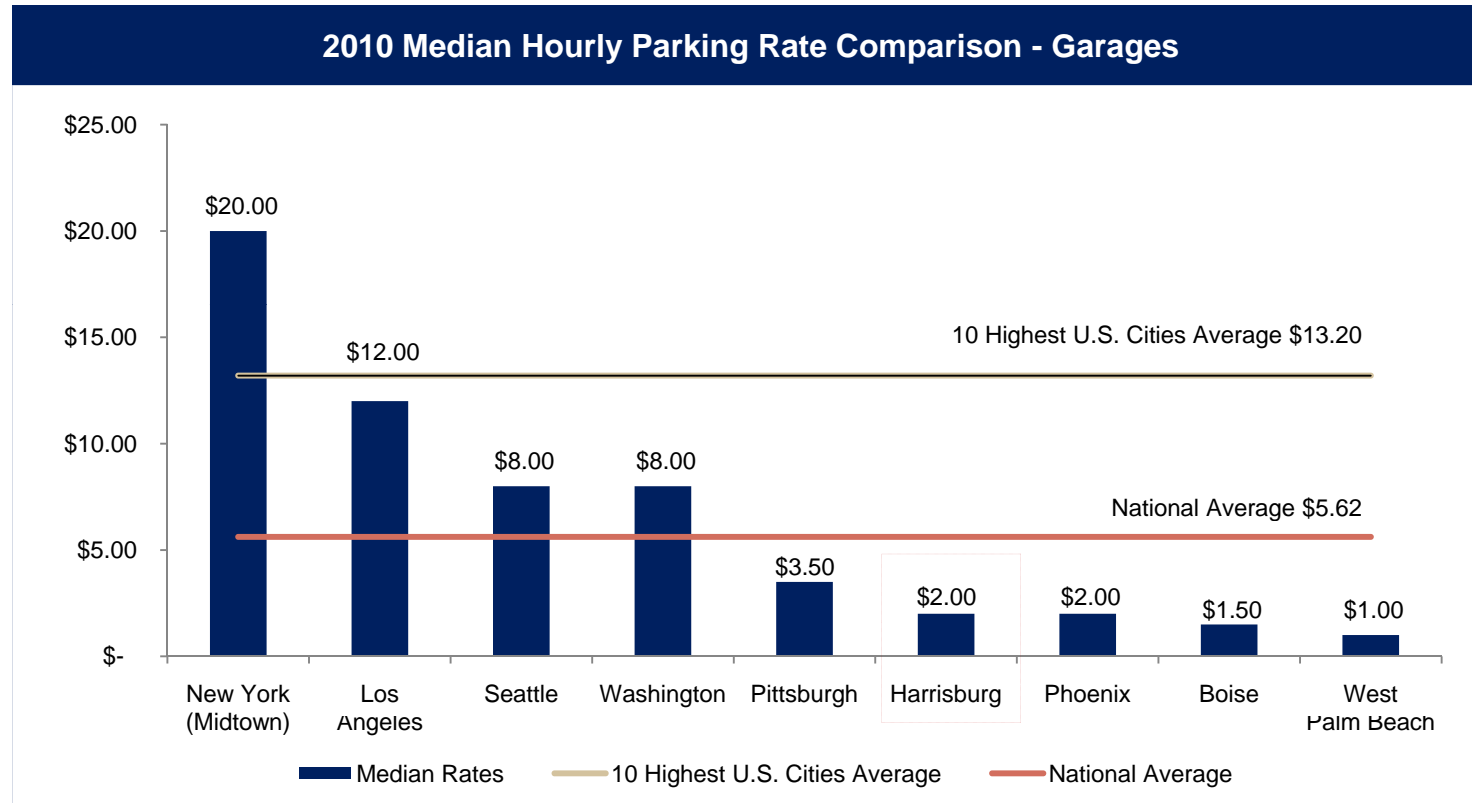
Harrisburg's daily parking rates are approximately 22% higher than the national average and approximately 49% lower than the 10 highest U.S. Cities average



Source: (a) Colliers 2010 North America Parking Rate Survey  
(b) City of Pittsburgh Public Parking System – Request for Concessionaire Qualifications  
(c) Harrisburg Parking Authority

## IV. Harrisburg Parking Authority Median Hourly Parking Rate Comparison

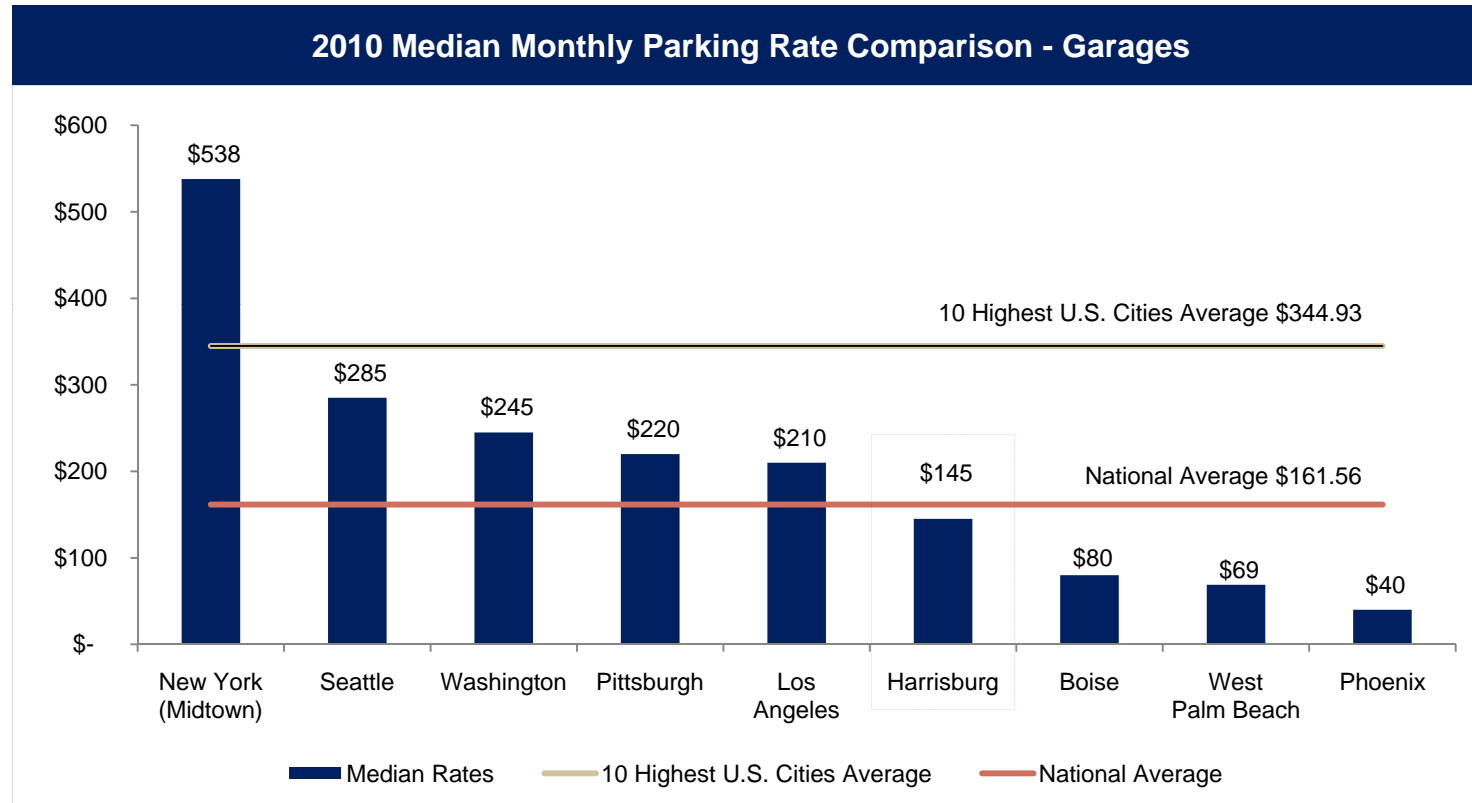
Harrisburg's hourly parking rates are significantly lower than both the national average and the 10 highest U.S. Cities average



Source: (a) Colliers 2010 North America Parking Rate Survey  
(b) City of Pittsburgh Public Parking System – Request for Concessionaire Qualifications  
(c) Harrisburg Parking Authority

## IV. Harrisburg Parking Authority Median Monthly Parking Rate Comparison

Harrisburg's monthly parking rates approximate the national average and are significantly lower than the 10 highest U.S. Cities average



Source: (a) Colliers 2010 North America Parking Rate Survey  
(b) City of Pittsburgh Public Parking System – Request for Concessionaire Qualifications  
(c) Harrisburg Parking Authority

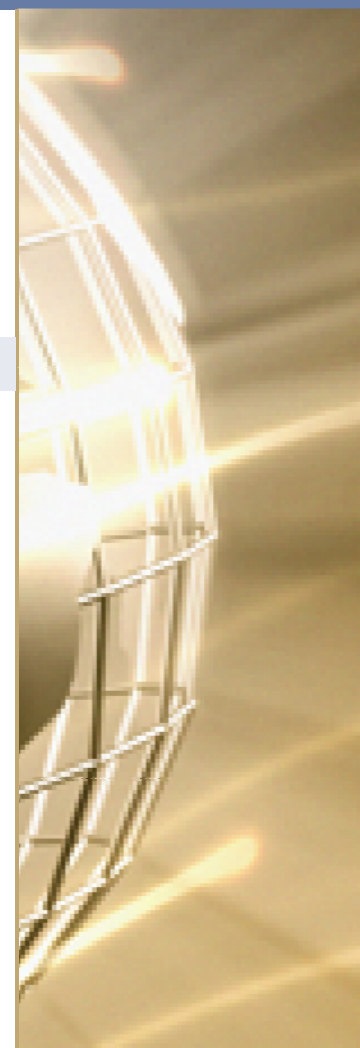
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## IV. Monetization Options – Resource Recovery Facility

Both the City and THA lack the necessary revenue to meet debt obligations related to the RRF

### Incinerator Background:

- ▲ Environmental retrofit took 5 years to meet environmental standards and exacerbated the debt problem
- ▲ Currently unable to generate projected revenue necessary for bond payments

### Debt payments are falling to guarantors:

- ▲ THA and then the City have the first responsibility for all debt payments, but cannot pay
- ▲ Debt Service Reserve Funds drawn down to zero for most issues
- ▲ County paying for issues 2003 D and E, and most notably was forced to pay \$35 million on the 2007 C & D Bonds
- ▲ AGM paying for 2002 A and 2003 F Bonds
- ▲ County, AGM, Incinerator operators, and guarantors have initiated litigation to recover amounts allegedly owed by the city

### Possible Alternatives:

- ▲ Concession/Lease of Facility: Current proposal from Leeward County, Incinerator Management Authority, (“LCSWMA”) of \$45 million without assuming debt obligation - need to run a formal process
- ▲ Operational Restructuring: Pursue revenue opportunities and cut costs where possible - an improved bottom line could allow refinancing
- ▲ Financial Restructuring: Restructure bonds to extend maturity and seek debt forgiveness either in or out of court

## IV. Monetization Options – Resource Recovery Facility

The RRF's projected 2011 Income of under \$6 million is insufficient to service current debt service (approximately \$18 million in 2011)

THA/RRF Budget					
(\$s in Millions)					
	2009		2010		2011
	Budgeted		Approved		Amended
Revenues:					
Tipping Fees	\$	20.34	\$	20.86	\$ 21.89
Electricity Sales		4.32		4.42	4.16
Ferrous Sales		0.18		0.43	0.65
Other Revenue		0.20		0.03	0.03
<b>Total Revenue</b>		<b>25.04</b>		<b>25.75</b>	<b>26.74</b>
Operating Expenses:					
Waste Transfer & Ash Disposal		3.45		3.27	3.38
Covanta		13.48		11.79	12.53
Fees to Municipalities		0.69		0.79	0.81
Environmental Steward / DEP Fees		0.48		0.60	0.65
Utilities		1.99		2.36	1.35
Risk Management		0.35		0.42	0.42
Permit Expenses		0.27		0.07	0.08
Other		0.74		0.24	0.06
<b>Total Operating Expenses</b>		<b>21.44</b>		<b>19.54</b>	<b>19.29</b>
<b>Operating Profit</b>	<b>\$</b>	<b>3.60</b>	<b>\$</b>	<b>6.22</b>	<b>\$ 7.45</b>
Non-Operating Expenses:					
Bank & Trustee Fees		-		0.14	0.05
Miscellaneous Expenses <sup>1</sup>		-		3.79	0.10
Insurance Consultant		-		0.02	0.01
Legal Fees		-		0.70	0.75
Engineering Fees		-		0.25	0.13
Facilities Management		-		0.22	0.25
Management Audit & Appraisal		-		0.11	-
Professional Fees - Arbitrage, Energy		-		0.15	0.15
Maintenance / Improvements		-		0.09	0.10
THA Administration Fees		-		0.30	0.30
Non-Operating Expenses		1.53		5.76	1.84
<b>Income Prior to Debt Service</b>	<b>\$</b>	<b>2.07</b>	<b>\$</b>	<b>0.46</b>	<b>\$ 5.61</b>

Sources: a. Data from THA website

Notes: 1. Still researching 2010 Miscellaneous Expenses

## IV. Monetization Options – Resource Recovery Facility

Based on discussions with various officials (including representatives of the County), there are several potential operating changes that could improve the RRF bottom line in the short term

- ▲ Specialty Waste Focus – With the RRF running at close to full capacity, management could focus on higher margin waste. Management could seek specialty waste opportunities that are more profitable than mainstream waste. Possibilities include modifying the contract with Covanta Harrisburg, Inc. (“Covanta”) to insert a revenue sharing provision to incentivize Covanta or renegotiating to give THA greater control in operations.
- ▲ Raise energy sales rate and volume – Currently selling electricity on spot market at approximately 4.5 cents per kilowatt/hour while City residents buy electricity from utilities at approximately 9.3 cents per kilowatt/hour<sup>1</sup>. Opportunity to petition the State/governing body to mandate the RRF to sell energy direct to consumers at both a lower rate than from a utility and at a higher rate than spot market (i.e. both parties benefit) under a green energy initiative. Additionally, this would lock in prices and potentially eliminate need for pricing/arbitrage consultant expenses of \$100,000 to \$150,000 per year.  
(1) Source: PPL Electric Utilities Corporation’s “General Tariff Rules and Rate Schedules for Electrical Service Effective March 17,2011
- ▲ Steam Unit – If further capital funds can be found, planned steam unit can be built and brought online, boosting RRF revenues. Estimated \$15 to \$20 million investment and will provide an estimated additional \$3 million of revenue per year.
- ▲ Ash Disposal – Currently paying \$3 million a year to dispose of ash. Need to investigate opportunities at State level to see if ash can be stored elsewhere at reduced cost. Can the State force neighboring landfills to accept ash?
- ▲ Legal Expense Reduction – Approximately \$750,000 per year can be reduced post-restructuring.

## IV. Monetization Options – Resource Recovery Facility

Given the potential operating improvements noted, profitability could be improved significantly, however, improvements alone will not address THA/RRF 2011 debt service amounts or its past due payments

**Note:** The following analysis is solely for illustrative purposes and is based on high-level discussions with various officials (including representatives of the County). Ultimately, the potential opportunities discussed herein need to be vetted through a formal review process.

### THA/RRF 2011 Pro-Forma

(\$s in Millions)	2011 Amended	Pro-forma Adjustments	2011 Pro-Forma	Note
<b>Revenues:</b>				
Tipping Fees	\$ 21.89	\$ 1.71	\$ 23.60	A
Electricity Sales	7.10	0.10	7.20	B
Ferrous Sales	0.65	-	0.65	
Other Revenue	0.03	3.00	3.03	C
<b>Total Revenue</b>	<b>26.74</b>	<b>8.47</b>	<b>35.21</b>	
<b>Operating Expenses:</b>				
Waste Transfer & Ash Disposal	3.38	(3.00)	0.38	D
Other Operating Expenses	15.91	-	15.91	
<b>Total Operating Expenses</b>	<b>19.29</b>	<b>(3.00)</b>	<b>16.29</b>	
<b>Operating Profit</b>	<b>\$ 7.45</b>	<b>\$ 11.47</b>	<b>\$ 18.92</b>	
<b>Non-Operating Expenses:</b>				
Legal Fees	0.75	(0.75)	-	E
Professional Fees - Arbitrage, Energy, Other	0.15	(0.15)	-	F
All Other Non-Operating Expenses	0.94	-	0.94	
Non-Operating Expenses	1.84	(0.90)	0.94	
<b>Income Prior to Debt Service</b>	<b>\$ 5.61</b>	<b>\$ 12.37</b>	<b>\$ 17.98</b>	

Sources: a. Data from THA website

#### A. Convert 50% of current county waste disposal (avg. \$73/ton) to specialty waste (avg. \$100/ton):

2011 Tons (50%)		\$/ton Increase		Pro-Forma Adjustment
63,325	x	\$27	=	\$ 1.71

#### B. Four cent increase in energy sales rate from current spot market (4.5 cents) to direct to consumer (est. 8.5 cents):

2011 kWh		\$/kWh Increase		Pro-Forma Adjustment
94	x	\$0.040	=	\$ 3.76

#### C. Steam unit revenue - assumes \$15 to \$20 million capital investment

#### D. Ash disposal savings

#### E. Legal expense savings

#### F. Pricing/Arbitrage consulting savings from set energy price to State

## IV. Monetization Options – Resource Recovery Facility

LCSWMA has proposed to enter a sale of the RRF for \$45 million

**Note:** The proposal discussed hereafter is presented solely to illustrate a potential sale structure and does not constitute an endorsement or recommendation. Should the City ultimately decide to pursue a sale, it should consider whether to undertake a competitive bid process.

### Key Provisions:

- ▲ Substantially all assets necessary for operation transferred to LCSWMA excluding the ash fill, free and clear of any liens (proposal explicitly states that LCSWMA will not assume any debt). This will require AGM and Covanta authorization.
- ▲ Consideration of \$45 million to THA, Lancaster must be able to finance \$40 million tax exempt for more than 20 years at 6.5%.
- ▲ All operating systems must have at least 23 years of expected useful life.
- ▲ RRF must be treated as tax exempt government operation.
- ▲ Exemption from existing and future litigation with Harrisburg parties.
- ▲ No obligation to retain employees.

### Tipping Fees:

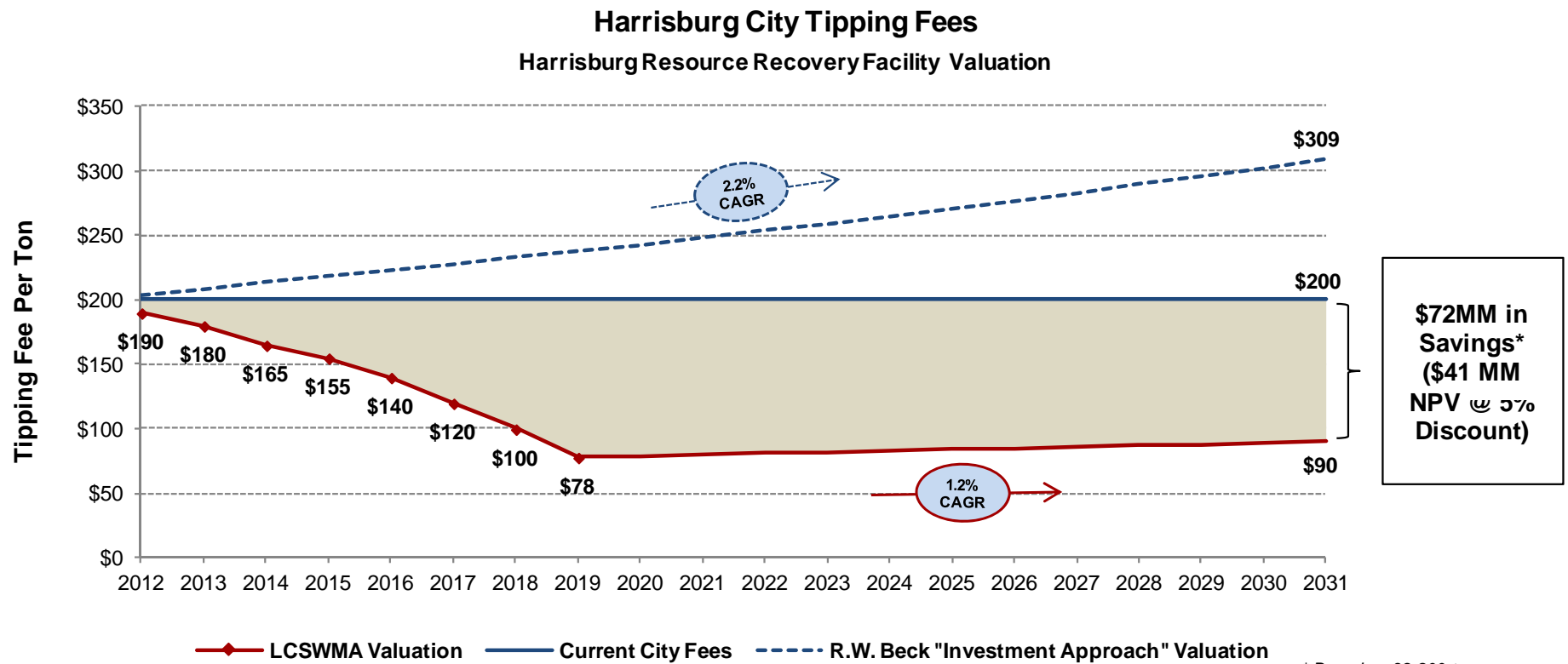
- ▲ Disputes City's above-market tipping rates and R. W. Beck, Inc.'s other valuation model assumptions.
- ▲ Notes possible difficulty in maintaining rates due to established US Supreme Court rulings in 1994 (*Carbone*) and 2007 (*United Haulers*).

### Effect to City:

- ▲ New tipping rates to save city residents \$13.6 million per year until 2019, expected total of \$113 million over 20 years.
- ▲ \$20 million in capital improvements over first 10 years.
- ▲ Will not develop on-site ash disposal.

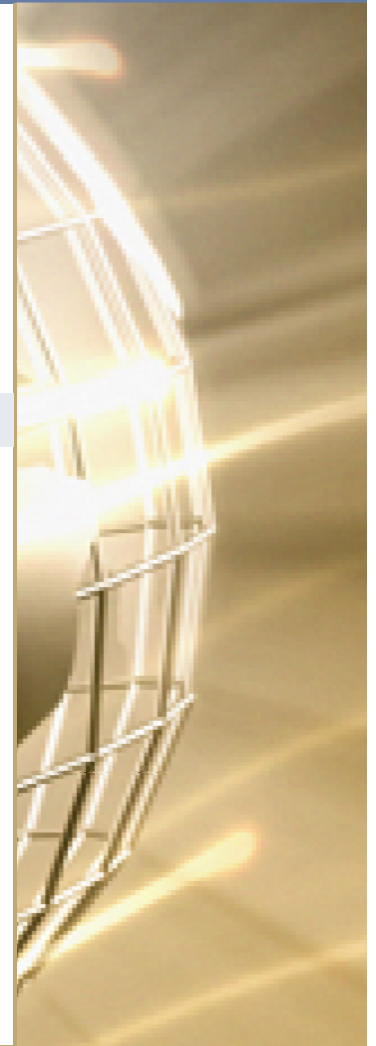
## IV. Monetization Options – Resource Recovery Facility

If the City has the ability to leave tipping fees unmodified, the City could potentially realize an additional \$72 million in revenue through 2031. Conversely, LCSWMA could adjust its up-front payment by at least \$41 million (the NPV of the estimated savings).



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## IV. Monetization Options – City Island

City Island monetization options are limited – potential opportunities to make City Island cash flow neutral need to be explored

**With the AA Baseball Team already sold, the City earns income largely off of the Baseball Stadium's permit fees, which are used to make debt service payments on the revenue bonds associated with the stadium (remaining principal of \$8 million).**

- ▲ However, attendance thresholds have not been met and City is currently subsidizing the Stadium Debt from the General Fund (approximately \$130,000 to \$250,000 per year).

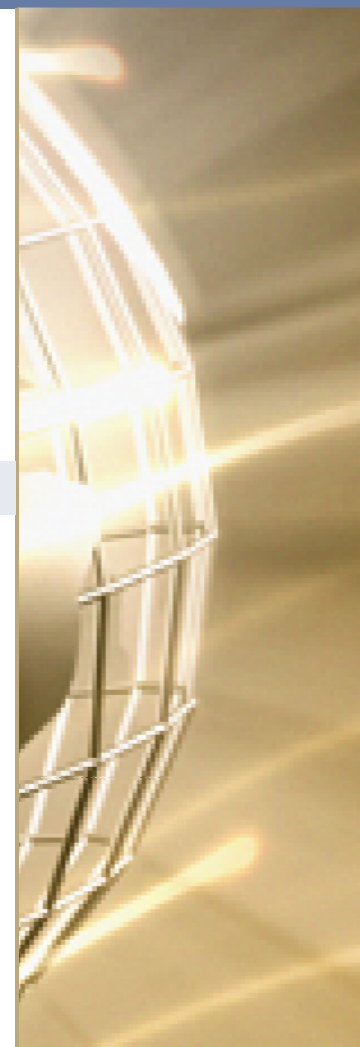
**Any sale/lease/development initiative would need to address the stadium debt shortfalls before any funds could flow through to General Fund. Given the current economic climate, it is unlikely that City Island will generate an investment large enough to provide any meaningful relief to the General Fund.**

City Island Historical P&L			
(\$s in Millions)			
	2008 Actual	2009 Actual	2010 Actual
<u>Revenues:</u>			
Permit Fee from AA Team	\$ 0.37	\$ 0.37	\$ 0.37
Naming Rights	0.10	0.07	0.07
Other Park Permit Fees	0.09	0.04	0.08
Other	0.01	0.18	(0.01)
<b>Total Revenue</b>	<b>0.56</b>	<b>0.66</b>	<b>0.52</b>
<u>Expenses:</u>			
Operating Expenses	0.14	0.22	0.11
Debt Service	0.55	0.65	0.65
<b>Surplus/(Deficit) After Debt</b>	<b>\$ (0.13)</b>	<b>\$ (0.21)</b>	<b>\$ (0.25)</b>

Sources: a. Data from City Controller's Office

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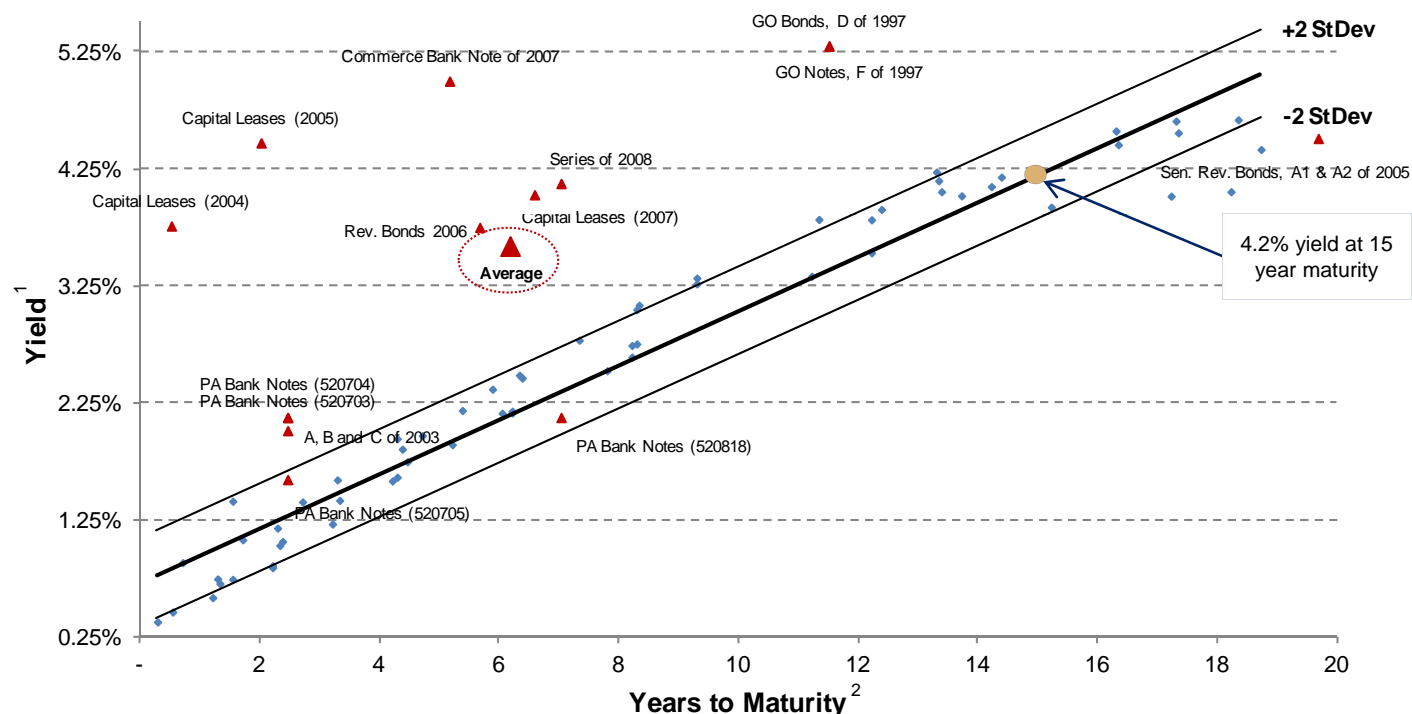
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## V. Debt Refinancing – Yield vs. Maturity Comparison (City Bonds)

Using current yields to maturity from a selection of recently issued bonds of other US capital cities, a newly issued municipal bond would require, on average, a 4.2% annual interest rate for 15 year maturity

Yield vs. Maturity (City Bonds)



- ◆ Selected recent issues for other US capital cities<sup>3</sup>
- ▲ City of Harrisburg

<sup>1</sup> Current yield to maturity is a reasonable approximation of new issue pricing given current market conditions and similar underlying risk parameters

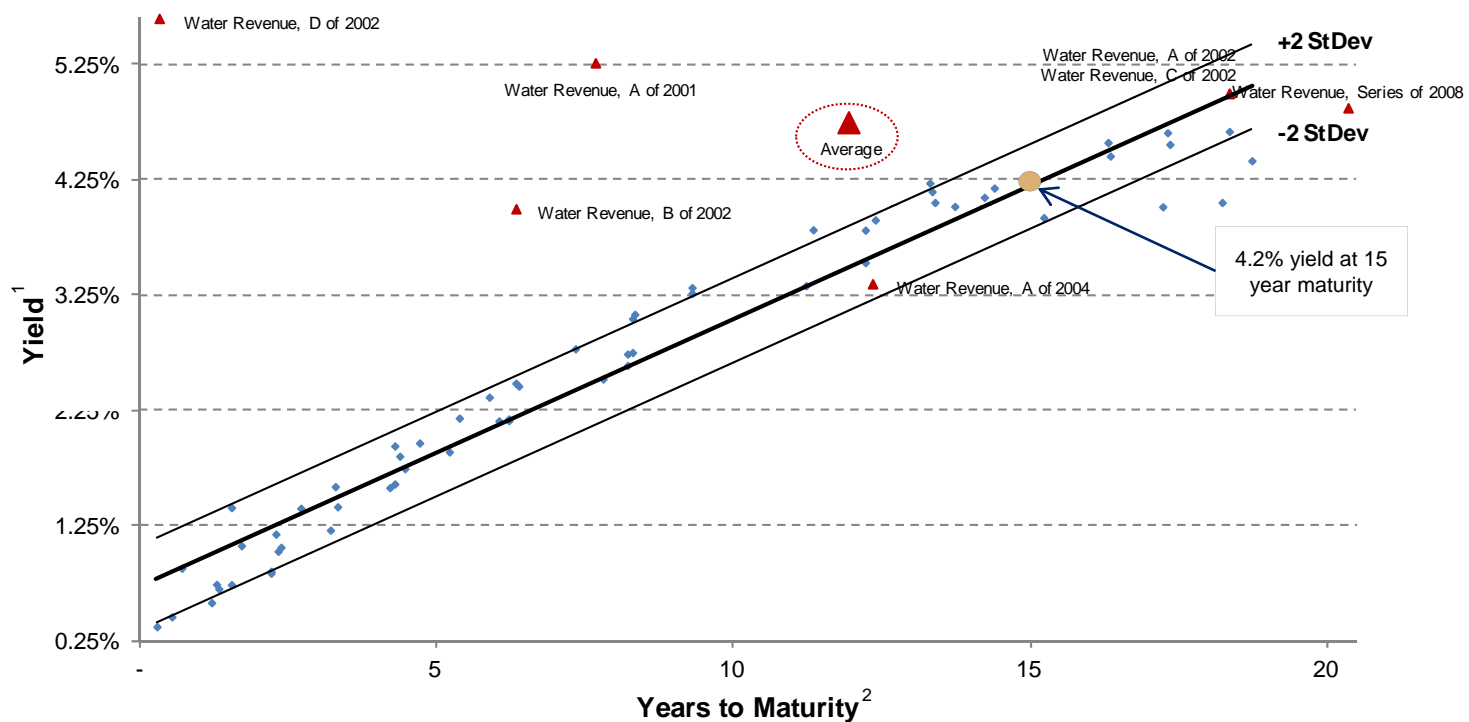
<sup>2</sup> Years to maturity calculated based on years left until maturity date (from 3/16/11)

<sup>3</sup> A selection of 61 bonds (A+ - AAA) from 8 capital cities; only non-insured federally tax exempt bonds

## V. Debt Refinancing – Yield vs. Maturity Comparison (Water Revenue Bonds)

Using current yields to maturity from a selection of recently issued bonds of other US capital cities, a newly issued municipal bond would require, on average, a 4.2% annual interest rate for 15 year maturity

**Yield vs. Maturity (Water Revenue Bonds)**



- ◆ Selected recent issues for other US capital cities<sup>3</sup>
- ▲ City of Harrisburg

<sup>1</sup> Current yield to maturity is a reasonable approximation of new issue pricing given current market conditions and similar underlying risk parameters

<sup>2</sup> Years to maturity calculated based on years left until maturity date (from 3/16/11)

<sup>3</sup> A selection of 61 bonds (A+ - AAA) from 8 capital cities; only non-insured federally tax exempt bonds

## V. Debt Refinancing

The City could benefit from refinancing the City debt and water revenue bonds to a 4.2% annual interest rate (average pricing of a 15-year issue)

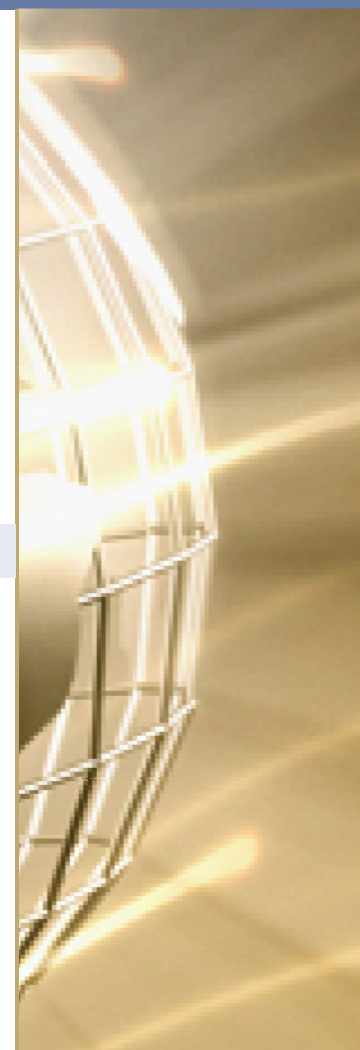
	Maturity Date	Yield to Maturity			Amount Outstanding 12/31/10	Annual Savings
		Current	New	Diff.		
<b>City Bonds</b>						
General Obligation Refunding Bonds, Series D of 1997	9/15/2022	5.3%	4.2%	-1.1%	\$ 17,415,619	\$ 191,572
General Obligation Refunding Notes, Series F of 1997	9/15/2022	5.3%	4.2%	-1.1%	17,415,619	191,572
Senators Revenue Bonds, Series A2 of 2005	11/15/2030	4.5%	4.2%	-0.3%	8,110,000	25,141
Capital Leases (2005)	3/23/2013	4.5%	4.2%	-0.3%	117,766	320
Commerce Bank Note of 2007	5/15/2016	5.0%	4.2%	-0.8%	3,980,982	31,848
						<b>\$ 440,453</b>
<b>Water Revenue Bonds</b>						
Water Revenue Bonds, Series A of 2001	11/15/2018	5.3%	4.2%	-1.1%	3,785,000	40,305
Water Revenue Bonds, Series A of 2002	7/15/2029	5.0%	4.2%	-0.8%	15,340,000	122,720
Water Revenue Bonds, Series C of 2002	7/15/2029	5.0%	4.2%	-0.8%	1,700,000	61,600
Water Revenue Bonds, Series D of 2002	7/15/2011	5.7%	4.2%	-1.5%	510,000	7,395
Water Revenue Bonds, Series of 2008	7/15/2031	4.9%	4.2%	-0.7%	69,420,000	468,585
						<b>\$ 700,605</b>
						<b>\$ 1,141,058</b>

**Note: 1. A&M Analysis does not account for changes in market trends, refinancing risks/costs and general credit risk for the underlying entity**

**Note: 2. Analysis assumes new issuance(s) is/are A+ to AAA rating or above, non-insured and federally tax-exempt**

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## VI. Tax and Other Considerations

Through the Act 47 process, the City may seek to increase taxes to increase revenue, although these taxes may be detrimental to the business environment and property values

Tax / Consideration	2011 Projected	Adjustable Out-of-Court	Adjustable Act 47	Treatment
Earned Income Tax ("EIT")	<b>\$3.1 million</b>		✓	Per Act 47, City may petition the Court of Common Pleas of the County to raise above statutory limits (1%) for one year. The court may renew such increase annually until the termination of Act 47 distressed status.
Real Estate Taxes	<b>\$18.1 million</b>		✓	Per Act 47, City may petition the Court of Common Pleas of the County to raise above statutory limits for one year. The court may renew such increase annually until the termination of Act 47 distressed status.
Emergency and Municipal Services Tax ("EMS")	<b>\$2.3 million</b>		✓	Allows municipalities to charge workers (including commuters) \$52 per day for emergency services. Harrisburg currently taxes approximately 68,000 workers.
Parking Tax	<b>\$1.9 million</b>	✓		Raising parking taxes may result in reduced commuters and thereby reduce revenue
Commuter Tax (Non-Resident EIT)	<b>N/A</b>		✓	The issue of a commuter tax has been raised before, but the County and State have legislative ability to deny.
Business Tax	<b>\$4.3 million</b>	✓	✓	Raising Business/Mercantile taxes may drive businesses out of Harrisburg

## VI. Tax and Other Considerations

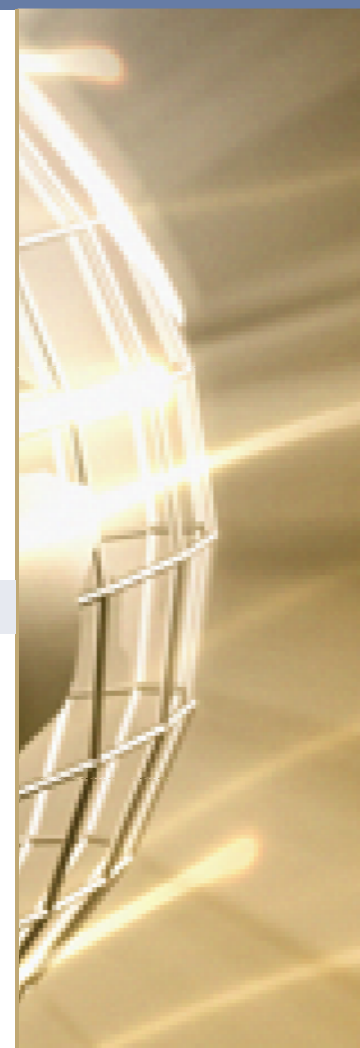
Through the Act 47 process, the City may seek to increase grants and PILOTs (from the Commonwealth of Pennsylvania and nonprofit organizations) or local fees

Tax / Consideration	2011 Projected	Adjustable Out-of-Court	Adjustable Act 47	Treatment
State Grants	<b>\$1.0 million</b>		✓	State grants currently paid to City for sanitation and liquid fuels. May be able to renegotiate with State given distressed situation.
State Pension Subsidy	<b>\$1.5 million</b>		✓	State grant currently paid to City for pensions. May be able to renegotiate with State given distressed situation.
PILOTs	<b>\$0.4 million</b>		✓	46% of Harrisburg's real estate is tax exempt, and PILOTs are given by the State/County for their use of real estate. In addition to possibly increasing their contributions, City may try to compel nonprofits to contribute more, though attempts have been unsuccessful in past
Capital Fire Protection (State Capital PILOT)	<b>\$0.9 million</b>		✓	Currently paid to City by State as a form of PILOT. May be able to renegotiate with State given distressed situation.
Parking/Traffic Fines & Forfeits	<b>\$2.4 million</b>	✓	✓	City may have room to increase parking penalties.
Building Permit Fees	<b>\$0.3 million</b>	✓	✓	Act 47 Coordinator looking potentially to increase fees across the City.
School Collection Fees	<b>\$0.1 million</b>	✓	✓	Act 47 Coordinator looking potentially to increase fees across the City.
Other Fees	<b>\$0.5 million</b>	✓	✓	Act 47 Coordinator looking potentially to increase fees across the City.



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## VII. Potential Restructuring Pro-Forma(s)

Using the proposals received for the City's parking system and the RRF as a benchmark, the City may be able to reduce its debt substantially, however, an additional \$15 million per year in cost reductions or revenue enhancements would need to be achieved to support the remaining THA/RRF debt service

**Note:** The following analysis is solely for illustrative purposes to present the impact of potential monetization alternatives and a hypothetical framework of a restructuring proposal. This analysis in no way endorses or recommends the sale or lease of any particular asset of the City or any other action.

Pro-forma Estimated THA/RRF Debt Service	
(\$ in millions)	Pro-forma
<b>Proceeds from Asset Monetizations:</b>	
Current HPA Offer from HPP <sup>1</sup>	\$ 215.00
Current RRF Proposal from LCSWMA <sup>1</sup>	45.00
<b>Total Proceeds from Asset Monetizations</b>	<b>\$ 260.00</b>
<b>Debt Reductions:</b>	
Defeasance of HPA Debt <sup>2</sup>	\$ (104.08)
Repayment of RRF Missed Payments <sup>2,3</sup>	(64.89)
Amount Remaining to Reduce RRF Principal <sup>4</sup>	(91.03)
<b>Total Debt Reductions</b>	<b>\$ (260.00)</b>
<b>Remaining Refinanced THA/RRF Debt</b>	
THA/RRF Principal Outstanding	\$ 241.62
Amount Remaining to Reduce RRF Principal <sup>2,4</sup>	(91.03)
<b>Total Remaining Refinanced THA/RRF Debt<sup>5</sup></b>	<b>\$ 150.59</b>
Refinancing Rate <sup>2,5</sup>	4.20%
<b>Annual Debt Service Required on Remaining THA/RRF Debt<sup>5</sup></b>	<b>\$ 13.73</b>

<b>Tipping Fee Adjustment<sup>6</sup></b>	
Net Present Value to City <sup>6</sup>	\$ (41.00)
Reduction to Debt Service <sup>2,5</sup>	\$ (3.74)

Pro-Forma Cash Flow Need to Service THA/RRF Debt	
(\$ in millions)	
<b>Debt Service after Asset Monetizations:</b>	
Debt Service on Remaining THA Debt <sup>2</sup>	\$ (13.73)
Loss of HPA Proceeds <sup>7</sup>	(2.29)
Refinance of General Fund Debt Savings <sup>2</sup>	0.44
Refinance of Water Fund Debt Savings <sup>2</sup>	0.70
<b>Free Cash Flow Needed to Service Remaining THA/RRF Debt</b>	
<b>(may be addressed thru Act 47 Actions)</b>	<b>\$ 14.88</b>
<b>Debt Service after Asset Monetizations &amp; Tipping Fee Adjustment:</b>	
Reduced Debt Service from Tipping Fee Adjustment <sup>6</sup>	\$ (3.74)
<b>Flow Needed to Service Remaining</b>	
<b>Tipping Fee Adjustment (may be addressed thru Act 47 Actions)</b>	<b>\$ 11.14</b>

Notes: 1. Current offers used for illustrative purposes only (see page 15 for HPA and page 27 for RRF)

2. Excludes transaction, refinancing, and defeasance costs

3. Includes \$16.8 million of missed payments from the DSRF; this assumes that refinanced principal will require new DSRFs

4. Assumes RRF proceeds plus excess HPA proceeds are applied to (i) RRF missed payments and then (ii) remaining RRF principal

5. Assumes remaining THA/RRF debt is refinanced / renegotiated and new issuance(s) is/are 15-year, A+ to AAA rating or above, non-insured, federally tax-exempt and reflect(s) a "sink" amortization structure with a portion of principal to be repaid each year

6. Reflects value to city from continuing to charge residents tipping fees at current rates (\$200/Ton) and paying contracted tipping fees, per proposal, to LCSWMA (reduction to THA/RRF debt may be effectuated through two alternatives: (i) an increased upfront payment from LCSWMA or (ii) from City using proceeds itself)

7. Proceeds forgone from City after HPA concession (see page 16)

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## VII. Potential Restructuring Pro-Forma(s)

Using the proposal received for the City's parking system and the improved RRF Pro-Forma Income Statement, the City may be able to reduce its debt substantially, however, an additional \$6 million per year in cost reductions or revenue enhancements would need to be achieved to support the remaining THA/RRF debt service

**Note:** The following analysis is solely for illustrative purposes to present the impact of potential monetization alternatives and a hypothetical framework of a restructuring proposal. This analysis in no way endorses or recommends the sale or lease of any particular asset of the City or any other action. Additionally, the Pro-Forma RRF Income Statement is based high-level discussions with various officials (including representatives of the County). Ultimately, potential opportunities need to be vetted through a formal review process.

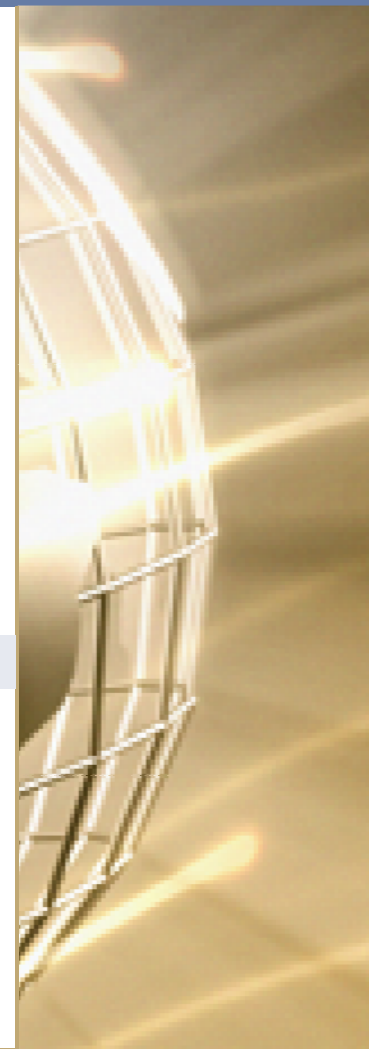
Pro-forma Estimated THA/RRF Debt Service (\$ in millions)	
	Pro-forma
<b>Proceeds from Asset Monetizations:</b>	
Current HPA Offer from HPP <sup>1</sup>	\$ 215.00
<b>Debt Reductions:</b>	
Defeasance of HPA Debt <sup>2</sup>	\$ (104.08)
Repayment of RRF Missed Payments <sup>2,3</sup>	(64.89)
Amount Remaining to Reduce RRF Principal <sup>4</sup>	(46.03)
<b>Total Debt Reductions</b>	<b>\$ (215.00)</b>
<b>Remaining Refinanced THA/RRF Debt</b>	
THA/RRF Principal Outstanding	\$ 241.62
Amount Remaining to Reduce RRF Principal <sup>2,4</sup>	(46.03)
<b>Total Remaining Refinanced THA/RRF Debt<sup>5</sup></b>	<b>\$ 195.59</b>
Refinancing Rate <sup>2,5</sup>	4.20%
<b>Annual Debt Service on Remaining THA/RRF Debt<sup>5</sup></b>	<b>\$ 17.84</b>

Pro-Forma Cash Flow Need to Service THA/RRF Debt (\$ in millions)	
<b>Debt Service after Asset Monetizations:</b>	
Debt Service on Remaining THA Debt <sup>2</sup>	\$(17.84)
Loss of HPA Proceeds <sup>6</sup>	(2.29)
RRF Pro-Forma Income Before Debt Service <sup>7,8</sup>	12.98
Refinance of General Fund Debt Savings <sup>2</sup>	0.44
Refinance of Water Fund Debt Savings <sup>2</sup>	0.70
<b>Free Cash Flow Needed to Service Remaining THA/RRF Debt (may be addressed thru Act 47 Actions)</b>	<b>\$ 6.00</b>

- Notes: 1. Current offers used for illustrative purposes only  
2. Excludes transaction, refinancing, and defeasance costs  
3. Includes \$16.8 million of missed payments from the DSRF; this assumes that refinanced principal will require new DSRFs  
4. Assumes RRF proceeds plus excess HPA proceeds are applied to (i) RRF missed payments and then (ii) remaining RRF principal  
5. Assumes remaining THA/RRF debt is refinanced / renegotiated and new issuance(s) is/are 15-year, A+ to AAA rating or above, non-insured, federally tax-exempt and reflect(s) a "sink" amortization structure with a portion of principal to be repaid each year  
6. Proceeds forgone from city after HPA concession (see page 16)  
7. Reflects Income Statement Pro-Forma reduced by \$3 million for steam unit revenue (i.e. assumes no capital investment) and \$2 million for capital expenditure reserve (see page 26)  
8. Pro-Forma adjustments based on high-level discussion with various officials and should be vetted through formal review process

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- VI. Tax & Other Considerations
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## VII. Appendix - City Budget Interfund Detail

### 2007 – 2011 City Budget Consolidated Budget

<b>City Budget Summary</b>					
<i>(\$s in Millions)</i>	2007	2008	2009	2010	2011
	Actual	Actual	Actual	Actual	Adopted
<u>Revenues:</u>					
General Fund Revenue	\$ 45.75	\$ 46.37	\$ 43.03	\$ 37.40	\$ 44.51
Water Fund Revenue	17.95	18.45	17.12	16.08	18.19
Sewer Fund Revenue	13.91	15.48	17.56	13.73	14.62
Sanitation Fund Revenue	4.26	4.37	4.39	4.12	4.47
State Liquid Fuels Fund Revenue	0.90	0.97	0.93	0.89	0.89
Other Revenue / Asset Sales	4.82	1.08	0.37	0.51	1.01
<b>Total City Revenue</b>	<b>87.58</b>	<b>86.72</b>	<b>83.40</b>	<b>72.74</b>	<b>83.70</b>
<u>Operating Expenses:</u>					
General Fund	49.28	47.48	48.56	40.63	44.79
Water Fund	3.79	3.84	3.76	3.36	4.02
Sewer Fund	6.01	5.74	5.54	4.87	7.40
Sanitation Fund	1.74	1.70	1.70	1.48	1.76
State Liquid Fuels Fund	0.85	0.90	0.84	0.75	0.89
<b>Total City Operating Expenses</b>	<b>61.67</b>	<b>59.66</b>	<b>60.39</b>	<b>51.08</b>	<b>58.85</b>
<b>Operating Surplus</b>	<b>\$ 25.90</b>	<b>\$ 27.06</b>	<b>\$ 23.01</b>	<b>\$ 21.66</b>	<b>\$ 24.84</b>
<u>Non-Operating Expenses:</u>					
Cap Ex	0.32	0.53	0.53	0.28	0.40
Debt Service (General Fund)	9.29	12.97	11.95	11.50	12.22
Debt Service (Water Fund)	8.17	-	8.90	13.18	10.88
Debt Service (Sewer Fund)	2.00	1.96	1.57	2.05	2.16
Non-Operating Expenses	19.78	15.46	22.95	27.01	25.66
<b>Surplus / Deficit</b>	<b>\$ 6.12</b>	<b>\$ 11.60</b>	<b>\$ 0.05</b>	<b>\$ (5.35)</b>	<b>\$ (0.82)</b>

Sources: a. Data from City Controller's Office; b. Water Fund Budget (THA)

## VII. Appendix - City Budget Interfund Detail

### 2007 – 2011 General Fund Budget

#### General Fund

(\$s in Millions)

	2007 Actual	2008 Actual	2009 Actual	2010 Actual	2011 Adopted
<b>Revenues:</b>					
Taxes	\$ 27.18	\$ 27.35	\$ 26.56	\$ 23.66	\$ 28.49
Interfund General Admin Charge	12.98	13.83	17.16	14.76	11.48
Departmental	6.14	6.08	5.10	4.58	5.34
Intergovernmental (State Grants)	4.19	3.88	3.55	3.68	2.58
HPA Transfer	4.01	4.75	4.05	2.19	4.00
Other Revenue	4.24	4.30	3.77	3.30	4.11
<b>Total Revenue</b>	<b>58.73</b>	<b>60.19</b>	<b>60.19</b>	<b>52.17</b>	<b>55.99</b>
<b>Operating Expenses:</b>					
General/Government	10.34	6.82	15.06	11.99	12.02
Administration	3.04	3.07	2.48	2.92	2.37
Building & Housing	0.94	1.06	0.88	0.91	0.93
Public Safety	26.84	28.22	23.23	20.56	23.18
Public Works	5.39	5.53	4.52	2.69	4.70
Parks & Recreation	2.74	2.78	2.39	1.57	1.58
<b>Total Operating Expenses</b>	<b>49.28</b>	<b>47.48</b>	<b>48.56</b>	<b>40.63</b>	<b>44.79</b>
<b>Non-Operating Expenses:</b>					
Debt Service	6.32	10.00	11.34	10.92	11.21
<b>Surplus / Deficit</b>	<b>\$ 3.13</b>	<b>\$ 2.71</b>	<b>\$ 0.30</b>	<b>\$ 0.62</b>	<b>\$ 0.00</b>

Sources: a. Data from City Controller's Office

## VII. Appendix - City Budget Interfund Detail

### 2007 – 2011 Water Fund Budget

<b>Water Fund</b>					
<i>(\$s in Millions)</i>	2007	2008	2009	2010	2011
	Actual	Actual	Actual	Actual	Adopted
<u>Revenues:</u>					
Water Sales	\$ 17.35	\$ 17.88	\$ 16.55	\$ 15.60	\$ 17.32
Fees	0.13	0.10	0.10	0.10	-
Investment Income	0.02	0.01	0.00	0.00	-
Meter/Valve Sales & Repairs	0.00	0.00	0.00	0.00	-
Other Revenue	0.45	0.46	0.45	0.38	0.87
THA - Transfers In					
<b>Total Revenue</b>	<b>17.95</b>	<b>18.45</b>	<b>17.12</b>	<b>16.08</b>	<b>18.19</b>
<u>Operating Expenses:</u>					
Administration	0.96	1.05	1.05	1.00	0.81
Distribution	0.85	0.80	0.76	0.66	0.98
Operations / Maintenance	1.98	1.99	1.96	1.70	2.24
General Fund Admin Expense	5.17	5.19	4.33	5.24	1.40
<b>Total Operating Expenses</b>	<b>8.96</b>	<b>9.03</b>	<b>8.10</b>	<b>8.59</b>	<b>5.42</b>
<u>Non-Operating Expenses:</u>					
Cap Ex	0.13	0.21	0.19	0.16	0.18
Debt Service	8.17	-	8.90	13.18	10.88
Non-Operating Expenses	8.30	0.21	9.09	13.34	11.06
<b>Surplus / Deficit</b>	<b>\$ ---</b>	<b>\$ 9.21</b>	<b>\$ (0.07)</b>	<b>\$ -.85</b>	<b>\$ 1.71</b>

Sources: a. Data from City Controller's Office; b. Water Fund Budget (THA)

## VII. Appendix - City Budget Interfund Detail

### 2007 – 2011 Sewer Fund Budget

Sewer Fund										
(\$s in Millions)										
		2007		2008		2009		2010		2011
		Actual		Actual		Actual		Actual		Adopted
<u>Revenues:</u>										
Sales to Public Authority	\$	7.20	\$	8.22	\$	7.33	\$	7.35	\$	7.94
Conveyance/Treatment		5.01		5.40		5.12		4.73		5.14
Investment Income		0.04		0.04		0.02		0.01		0.00
Collection/Sludge Handling		1.38		1.28		1.41		1.56		1.64
Other Revenue		0.28		0.54		0.49		0.09		(0.10)
THA - Transfers In		-		-		3.20		-		-
<b>Total Revenue</b>		<b>13.91</b>		<b>15.48</b>		<b>17.56</b>		<b>13.73</b>		<b>14.62</b>
<u>Operating Expenses:</u>										
Administration		1.31		1.16		1.12		1.03		1.38
Operations		0.00		0.00		0.00		0.00		0.00
Maintenance		0.79		0.83		0.83		0.64		0.88
Sewer Field Maintenance		0.62		0.54		0.43		0.39		0.53
General Admin Charges		5.49		6.32		10.13		7.28		7.28
<b>Total Operating Expenses</b>		<b>11.50</b>		<b>12.06</b>		<b>15.66</b>		<b>12.14</b>		<b>14.67</b>
<u>Non-Operating Expenses:</u>										
Cap Ex		0.05		0.10		0.01		-		0.08
Debt Service		2.00		1.96		1.57		2.05		2.16
Non-Operating Expenses		2.05		2.06		1.57		2.05		2.24
<b>Surplus / Deficit</b>	<b>\$</b>	<b>2.41</b>	<b>\$</b>	<b>1.36</b>	<b>\$</b>	<b>1.92</b>	<b>\$</b>	<b>(0.47)</b>	<b>\$</b>	<b>2.21</b>
Sources: a. Data from City Controller's Office; b. "CITY BUDGET HISTORICALS.xls"										



## VII. Appendix - City Budget Interfund Detail

### 2007 – 2011 Sanitation Fund Budget

<b>Sanitation Fund</b>										
<i>(\$s in Millions)</i>										
		2007		2008		2009		2010		2011
		Actual		Actual		Actual		Actual		Adopted
<u>Revenues:</u>										
Garbage Collection	\$	4.09	\$	4.14	\$	4.22	\$	3.95	\$	4.32
Grant Proceeds		0.10		0.14		0.14		0.13		0.13
Investment Income		0.02		0.01		0.00		0.00		0.00
Other Revenue		0.05		0.08		0.02		0.04		0.02
THA - Transfers In		-		-		-		-		-
<b>Total Revenue</b>		<b>4.26</b>		<b>4.37</b>		<b>4.39</b>		<b>4.12</b>		<b>4.47</b>
<u>Operating Expenses:</u>										
Administration		1.60		1.55		1.58		1.36		1.58
Operations / Maintenance		0.13		0.15		0.11		0.12		0.18
General Fund Transfers		2.33		2.32		2.70		2.25		2.81
<b>Total Operating Expenses</b>		<b>4.06</b>		<b>4.02</b>		<b>4.40</b>		<b>3.73</b>		<b>4.57</b>
<u>Non-Operating Expenses:</u>										
Cap Ex		0.15		0.23		0.34		0.11		0.15
Debt Service		-		-		-		-		-
Non-Operating Expenses		0.15		0.23		0.34		0.11		0.15
<b>Surplus / Deficit</b>	<b>\$</b>	<b>0.05</b>	<b>\$</b>	<b>0.13</b>	<b>\$</b>	<b>(0.35)</b>	<b>\$</b>	<b>0.28</b>	<b>\$</b>	<b>(0.24)</b>

Sources: a. Data from Cit. Controller's Office. b. "CITY BUDGET HISTORICALS.xls"

## VII. Appendix - City Budget Interfund Detail

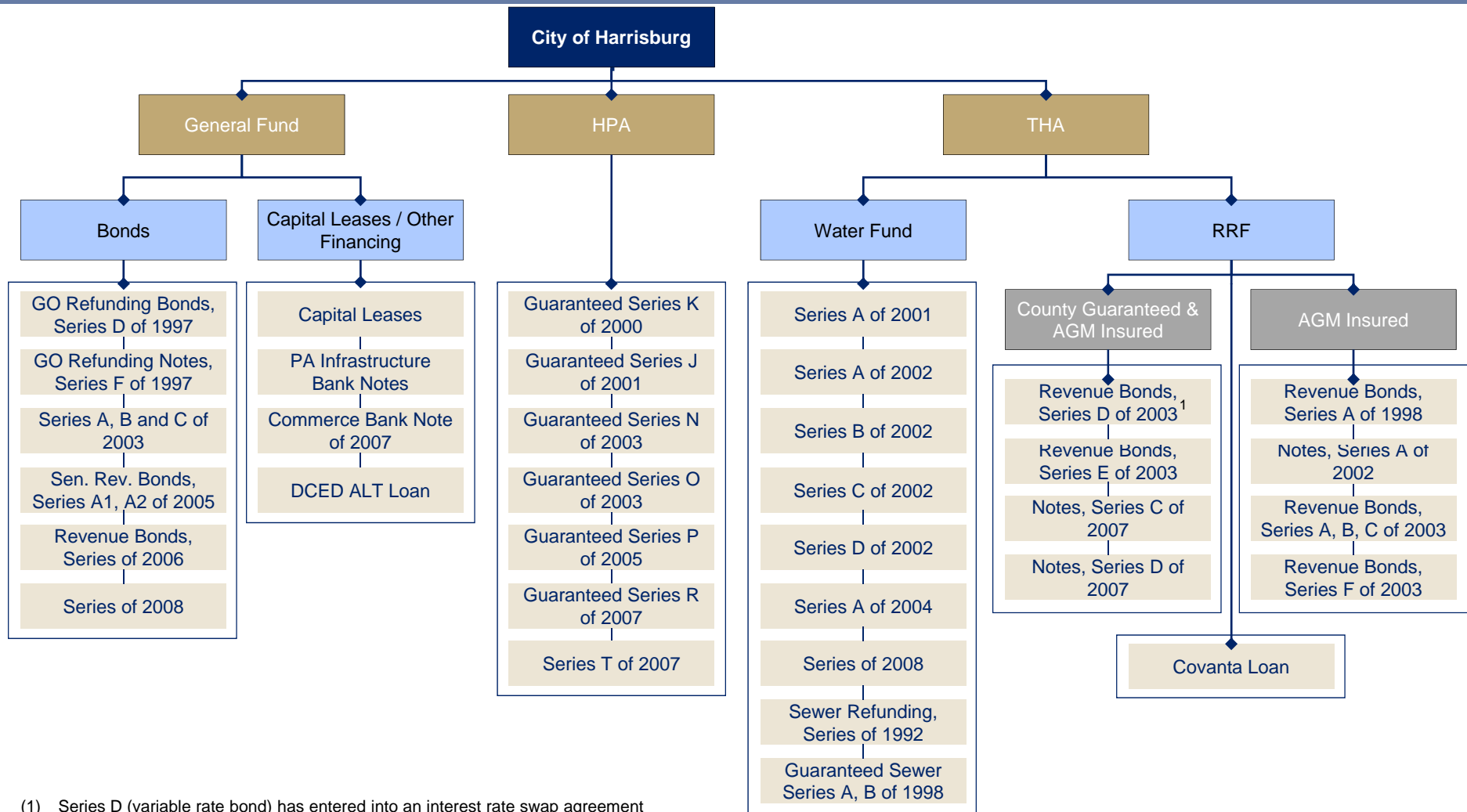
### 2007 – 2011 Liquid Fuels Fund Budget

Liquid Fuels Fund									
(\$s in Millions)									
		2007		2008		2009		2010	2011
		Actual		Actual		Actual		Actual	Adopted
<u>Revenues:</u>									
Grant Proceeds	\$	0.87	\$	0.96	\$	0.93	\$	0.89	0.89
Investment Income		0.03		0.01		0.00		0.00	0.00
THA - Transfers ...		-		-		-		-	-
<b>Total Revenue</b>		<b>0.90</b>		<b>0.97</b>		<b>0.93</b>		<b>0.89</b>	<b>0.89</b>
<u>Operating Expenses:</u>									
Operations / Maintenance		0.85		0.90		0.84		0.75	0.89
General Fund Admin Expense		-		-		-		-	-
<b>Total Operating Expenses</b>		<b>0.85</b>		<b>0.90</b>		<b>0.84</b>		<b>0.75</b>	<b>0.89</b>
<u>Non-Operating Expenses:</u>									
Debt Service (General Fund)		0.06		0.07		0.07		0.07	-
<b>Surplus / Deficit</b>	\$	<b>(0.01)</b>	\$	<b>0.01</b>	\$	<b>0.02</b>	\$	<b>0.08</b>	<b>-</b>

Sources: a. Data from City Controller's Office; b. "CITY BUDGET HISTORICALS.xls"

# VII. Appendix – Debt Structure

## City Debt Flow Chart



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## VII. Appendix – Debt Structure

### City & Resource Recovery Facility Debt Balances

City Debt	Principal Outstanding	Remaining Proj. Interest		Missed Payments	Principal Outstanding	Total Outstanding	Total with Proj. Interest
		2011	After 2011				
GO Refunding Bonds, Series D of 1997	\$ 17,415,619	\$ 2,264,961	\$ 25,514,420	\$ -	\$ 17,415,619	\$ 17,415,619	\$ 45,195,000
GO Refunding Notes, Series E of 1997	20,817,338	2,103,699	35,848,963	-	20,817,338	20,817,338	58,770,000
Series A, B and C of 2003	201,629	4,058	4,112	-	201,629	201,629	209,799
Sen. Rev. Bonds, Series A2 of 2005	8,110,000	408,330	4,503,899	-	8,110,000	8,110,000	13,022,228
Revenue Bonds, Series of 2006	5,310,000	-	765,326	-	5,310,000	5,310,000	6,075,326
Series of 2008	1,994,317	82,266	305,357	-	1,994,317	1,994,317	2,381,939
Pennsylvania Infrastructure Bank Notes	2,196,137	86,327	309,473	-	2,196,137	2,196,137	2,591,937
Capital Leases	5,166,094	1,446,612	3,322,364	-	5,166,094	5,166,094	9,935,069
Commerce Bank Note of 2007	3,980,982	181,545	412,602	-	3,980,982	3,980,982	4,575,130
DCED ALT Loan	21,630	1,845	-	-	21,630	21,630	23,475
<b>Total</b>	<b>\$ 65,213,746</b>	<b>\$ 6,579,641</b>	<b>\$ 70,986,514</b>	<b>\$ -</b>	<b>\$ 65,213,746</b>	<b>\$ 65,213,746</b>	<b>\$ 142,779,902</b>

Guaranteed/Insured THA/RRF Debt	Principal Outstanding	Remaining Proj. Interest		Missed Payments	Principal Outstanding	Total Outstanding	Total with Proj. Interest
		2011	After 2011				
Revenue Bonds, Series A of 1998 <sup>1</sup>	\$ 11,165,000	\$ 558,250	\$ 3,760,500	\$ 600,170	\$ 11,165,000	\$ 11,765,170	\$ 16,083,920
Notes, Series A of 2002	14,080,000	805,376	4,972,110	2,440,489	14,080,000	16,520,489	22,297,975
Revenue Bonds, Series A, B, C of 2003	75,925,000	3,315,762	70,320,068	5,218,203	75,925,000	81,143,203	154,779,033
Revenue Bonds, Series D of 2003 <sup>2</sup>	96,480,000	6,398,000	93,249,750	12,793,465	96,480,000	109,273,465	208,921,215
Revenue Bonds, Series E of 2003	11,655,000	579,457	1,786,690	3,715,879	11,655,000	15,370,879	17,737,027
Revenue Bonds, Series F of 2003	11,280,000	566,490	1,751,085	3,523,716	11,280,000	14,803,716	17,121,291
Notes, Series C of 2007	-	-	-	23,920,000	-	23,920,000	23,920,000
Notes, Series D of 2007	-	-	-	10,765,000	-	10,765,000	10,765,000
Covanta Loan	21,037,500	148,219	2,159,010	1,912,500	21,037,500	22,950,000	25,257,229
<b>Total</b>	<b>\$ 241,622,500</b>	<b>\$ 12,371,554</b>	<b>\$ 177,999,213</b>	<b>\$ 64,889,423</b>	<b>\$ 241,622,500</b>	<b>\$ 306,511,923</b>	<b>\$ 496,882,690</b>

Sources: a. Payment schedules provided by City Controller's Office; b. Past due data from indenture trustees; c. Covanta Complaint

Notes: 1. Indenture trustee would not provide information; data from 2008 audit

2. Missed payments include amounts paid by County on RBC swap agreement

## VII. Appendix – Debt Structure

### Parking, Water & Sewer Debt Balances

Parking Revenue Bonds	Principal Outstanding	Remaining Proj. Interest		Missed Payments	Principal Outstanding	Total Outstanding	Total with Proj. Interest
		2011	After 2011				
Guaranteed Series K of 2000	\$ 11,800,000	\$ 944,000	\$ 11,392,000	\$ -	\$ 11,800,000	\$ 11,800,000	\$ 24,136,000
Guaranteed Series J of 2001	27,350,000	1,345,736	10,475,176	-	27,350,000	27,350,000	39,170,913
Guaranteed Series N of 2003	4,090,000	166,195	438,920	-	4,090,000	4,090,000	4,695,115
Guaranteed Series O of 2003	9,010,000	420,885	1,334,850	-	9,010,000	9,010,000	10,765,735
Guaranteed Series P of 2005	16,565,000	879,158	12,669,068	-	16,565,000	16,565,000	30,113,225
Guaranteed Series R of 2007	16,625,000	736,342	10,966,401	-	16,625,000	16,625,000	28,327,743
Series T of 2007	18,640,000	758,616	7,976,386	-	18,640,000	18,640,000	27,375,002
<b>Total</b>	<b>\$ 104,080,000</b>	<b>\$ 5,250,932</b>	<b>\$ 55,252,801</b>	<b>\$ -</b>	<b>\$ 104,080,000</b>	<b>\$ 104,080,000</b>	<b>\$ 164,583,733</b>

Water & Sewer Revenue Bonds	Principal Outstanding	Remaining Proj. Interest		Missed Payments	Principal Outstanding	Total Outstanding	Total with Proj. Interest
		2011	After 2011				
Series A of 2001	\$ 3,785,000	\$ 199,275	\$ 481,313	\$ -	\$ 3,785,000	\$ 3,785,000	\$ 4,465,588
Series A of 2002	15,340,000	767,000	10,021,250	-	15,340,000	15,340,000	26,128,250
Series B of 2002	23,035,000	921,400	3,277,400	-	23,035,000	23,035,000	27,233,800
Series C of 2002	7,700,000	385,000	6,930,000	-	7,700,000	7,700,000	15,015,000
Series D of 2002	510,000	28,815	-	-	510,000	510,000	538,815
Series A of 2004	36,795,000	1,825,060	17,030,203	-	36,795,000	36,795,000	55,650,263
Series of 2008	69,420,000	3,555,300	61,724,550	-	69,420,000	69,420,000	134,699,850
Sewer Refunding, Series of 1992	901,780	1,264,042	1,294,178	-	901,780	901,780	3,460,000
Guaranteed Series of 1998	1,630,744	78,374	266,612	-	1,630,744	1,630,744	1,975,730
<b>Total</b>	<b>\$ 159,117,524</b>	<b>\$ 9,024,266</b>	<b>\$ 101,025,505</b>	<b>\$ -</b>	<b>\$ 159,117,524</b>	<b>\$ 159,117,524</b>	<b>\$ 269,167,295</b>

Sources: a. Payment schedules provided by City Controller's Office; b. Water/Sewer schedules from Milt Lopus Associates file

## VII. Appendix – Debt Structure

### Resource Recovery Facility – Past Due and 2011 Payments

County Guaranteed	Past Due					2011 Principal	2011 Interest	2011 Current Total	Grand Total
	DSRF	County	AGM	Past Due					
Revenue Bonds, Series D of 2003 <sup>1</sup>	\$ 8,002,547	\$ 4,790,919	\$ -	\$ 12,793,465	\$ -	\$ 6,398,000	\$ 6,398,000	\$ 19,191,465	
Revenue Bonds, Series E of 2003	1,099,520	2,616,359	-	3,715,879	1,520,000	579,457	2,099,457	5,815,337	
Notes, Series C of 2007	-	23,920,000	-	23,920,000	-	-	-	23,920,000	
Notes, Series D of 2007	-	10,765,000	-	10,765,000	-	-	-	10,765,000	
Total	\$ 9,102,067	\$ 42,092,278	\$ -	\$ 51,194,345	\$ 1,520,000	\$ 6,977,457	\$ 8,497,457	\$ 59,691,802	
AGM Insured									
Revenue Bonds, Series A of 1998 <sup>2</sup>	600,170	-	-	600,170	-	558,250	\$ 558,250	\$ 1,158,420	
Notes, Series A of 2002	800,013	-	1,640,476	2,440,489	840,000	805,376	1,645,376	4,085,865	
Revenue Bonds, Series A, B, C of 2003	5,218,203	-	-	5,218,203	-	3,315,762	3,315,762	8,533,965	
Revenue Bonds, Series F of 2003	1,124,304	-	2,399,413	3,523,716	1,465,000	566,490	2,031,490	5,555,206	
Total	\$ 7,742,690	\$ -	\$ 4,039,888	\$ 11,782,578	\$ 2,305,000	\$ 5,245,877	\$ 7,550,877	\$ 19,333,456	
Covanta Loan (City Backed)	-	-	-	1,912,500	1,888,472	148,219	2,036,691	3,949,191	
Total THA/RRF Debt Service	\$ 16,844,757	\$ 42,092,278	\$ 4,039,888	\$ 64,889,423	\$ 5,713,472	\$ 12,371,554	\$ 18,085,026	\$ 82,974,449	

Sources: a. Payment schedules provided by City Controller's Office; b. Past due data from indenture trustees; c. Covanta Complaint

Notes: 1. Past due include amounts paid by County on RBC swap agreement

2. Indenture trustee would not provide information, data from 2008 audit

## VII. Appendix – City Cash Detail

As of 3/17/11

City Cash Balances	
(\$s in Millions)	As of March 17, 2011
<u>Unrestricted</u>	
General Fund	\$ 2.58
Trust and Agency	0.85
Capital Projects	0.56
Debt Service	0.07
Sanitation Fund	0.32
Property Management	0.06
Total Unrestricted	4.45
<u>Restricted</u>	
Water Fund	0.53
RRF	0.00
Sewer Fund	1.76
State Liquid Fuels Fund	0.31
Total Unrestricted	2.60
<u>State &amp; Federal Funds Related</u>	
State Grants	1.04
Community Development Block Grant (CDBG)	0.34
Homeless Program	0.06
Federal Loan (Section 108)	1.85
Led Based Paint Relief Fund	0.07
Total State & Federal Funds Related	3.36
<b>Total City Cash Register</b>	<b>10.41</b>

## VII. Appendix – Bond Pricing Comparables

### Selection of Comparable Capital Bonds based on recent transactions

Name	State	Coupon	Maturity Date	Years to		Issue Date	Ratings				Issue Type	Tax Provision	Insured
				Maturity	Yield to Maturity		Composite	S&P	Moody	Fitch			
DOVER DEL ELEC REV	DE	5.00%	7/1/2015	4.3	1.944%	11/17/2010	AA-	NA	Aa2	A+	REVENUE BONDS	FED & ST TAX-EXEMPT	N
DOVER DEL ELEC REV	DE	4.25%	7/1/2019	8.3	3.048%	7/1/2008	AA-	NA	Aa2	A+	REVENUE BONDS	FED & ST TAX-EXEMPT	N
DOVER DEL ELEC REV	DE	2.00%	7/1/2011	0.3	0.378%	11/17/2010	AA-	NA	Aa2	A+	REVENUE BONDS	FED & ST TAX-EXEMPT	N
DOVER DEL ELEC REV	DE	2.00%	7/1/2012	1.3	0.745%	11/17/2010	AA-	NA	Aa2	A+	REVENUE BONDS	FED & ST TAX-EXEMPT	N
DOVER DEL ELEC REV	DE	3.00%	7/1/2013	2.3	1.180%	11/17/2010	AA-	NA	Aa2	A+	REVENUE BONDS	FED & ST TAX-EXEMPT	N
DOVER DEL ELEC REV	DE	4.00%	7/1/2014	3.3	1.592%	11/17/2010	AA-	NA	Aa2	A+	REVENUE BONDS	FED & ST TAX-EXEMPT	N
DOVER DEL ELEC REV	DE	4.50%	7/1/2024	13.3	4.223%	7/1/2008	AA-	NA	Aa2	A+	REVENUE BONDS	FED & ST TAX-EXEMPT	N
DOVER DEL ELEC REV	DE	5.00%	7/1/2027	16.3	4.574%	7/1/2008	AA-	NA	Aa2	A+	REVENUE BONDS	FED & ST TAX-EXEMPT	N
DOVER DEL ELEC REV	DE	4.25%	7/1/2020	9.3	3.317%	7/1/2008	AA-	NA	Aa2	A+	REVENUE BONDS	FED & ST TAX-EXEMPT	N
DOVER DEL ELEC REV	DE	5.00%	7/1/2028	17.3	4.659%	7/1/2008	AA-	NA	Aa2	A+	REVENUE BONDS	FED & ST TAX-EXEMPT	N
ALBANY NY	NY	4.00%	7/1/2020	9.3	3.268%	7/1/2009	NA	AA-	NA	NA	GENERAL OBLIGATION UNLTD	FED & ST TAX-EXEMPT	N
ALBANY NY	NY	NA	8/1/2013	2.4	1.066%	3/17/2011	NA	AA-	NA	NA	GENERAL OBLIGATION UNLTD	NA	N
ALBANY NY	NY	NA	8/1/2015	4.4	1.855%	3/17/2011	NA	AA-	NA	NA	GENERAL OBLIGATION UNLTD	NA	N
ALBANY NY	NY	NA	8/1/2016	5.4	2.185%	3/17/2011	NA	AA-	NA	NA	GENERAL OBLIGATION UNLTD	NA	N
ALBANY NY	NY	NA	8/1/2017	6.4	2.463%	3/17/2011	NA	AA-	NA	NA	GENERAL OBLIGATION UNLTD	NA	N
ALBANY NY	NY	NA	8/1/2023	12.4	3.903%	3/17/2011	NA	AA-	NA	NA	GENERAL OBLIGATION UNLTD	NA	N
ALBANY NY	NY	NA	8/1/2024	13.4	4.055%	3/17/2011	NA	AA-	NA	NA	GENERAL OBLIGATION UNLTD	NA	N
ALBANY NY	NY	NA	8/1/2025	14.4	4.180%	3/17/2011	NA	AA-	NA	NA	GENERAL OBLIGATION UNLTD	NA	N
ALBANY NY	NY	NA	12/1/2015	4.7	1.970%	3/17/2011	NA	AA-	NA	NA	GENERAL OBLIGATION UNLTD	NA	N
COLUMBUS OHIO	OH	2.00%	6/1/2015	4.2	1.583%	8/12/2010	AAA	AAA	Aaa	AAA	GENERAL OBLIGATION LTD	FED & ST TAX-EXEMPT	N
COLUMBUS OHIO	OH	3.38%	7/1/2019	8.3	2.754%	11/19/2009	AAA	AAA	Aaa	AAA	GENERAL OBLIGATION LTD	FED & ST TAX-EXEMPT	N
COLUMBUS OHIO	OH	3.00%	6/1/2013	2.2	0.858%	12/7/2010	AAA	AAA	Aaa	AAA	GENERAL OBLIGATION LTD	FED & ST TAX-EXEMPT	N
COLUMBUS OHIO	OH	3.00%	6/1/2014	3.2	1.215%	12/7/2010	AAA	AAA	Aaa	AAA	GENERAL OBLIGATION LTD	FED & ST TAX-EXEMPT	N
COLUMBUS OHIO	OH	3.00%	6/1/2016	5.2	1.893%	12/7/2010	AAA	AAA	Aaa	AAA	GENERAL OBLIGATION LTD	FED & ST TAX-EXEMPT	N
COLUMBUS OHIO	OH	3.00%	6/1/2017	6.2	2.179%	12/7/2010	AAA	AAA	Aaa	AAA	GENERAL OBLIGATION LTD	FED & ST TAX-EXEMPT	N
COLUMBUS OHIO	OH	3.00%	6/1/2019	8.2	2.741%	12/7/2010	AAA	AAA	Aaa	AAA	GENERAL OBLIGATION LTD	FED & ST TAX-EXEMPT	N
COLUMBUS OHIO	OH	3.50%	6/1/2023	12.2	3.815%	12/7/2010	AAA	AAA	Aaa	AAA	GENERAL OBLIGATION LTD	FED & ST TAX-EXEMPT	N
COLUMBUS OHIO	OH	3.75%	6/1/2025	14.2	4.099%	12/7/2010	AAA	AAA	Aaa	AAA	GENERAL OBLIGATION LTD	FED & ST TAX-EXEMPT	N
RICHMOND VA	VA	4.00%	7/15/2017	6.3	2.487%	11/30/2010	AA	AA	Aa2	AA+	GENERAL OBLIGATION UNLTD	FED & ST TAX-EXEMPT	N
RICHMOND VA	VA	4.00%	7/15/2018	7.3	2.786%	11/30/2010	AA	AA	Aa2	AA+	GENERAL OBLIGATION UNLTD	FED & ST TAX-EXEMPT	N
RICHMOND VA	VA	4.00%	7/15/2019	8.3	3.085%	11/30/2010	AA	AA	Aa2	AA+	GENERAL OBLIGATION UNLTD	FED & ST TAX-EXEMPT	N
RICHMOND VA	VA	5.00%	7/15/2027	16.3	4.457%	11/30/2010	AA	AA	Aa2	AA+	GENERAL OBLIGATION UNLTD	FED & ST TAX-EXEMPT	N
RICHMOND VA	VA	5.00%	7/15/2028	17.3	4.558%	11/30/2010	AA	AA	Aa2	AA+	GENERAL OBLIGATION UNLTD	FED & ST TAX-EXEMPT	N
RICHMOND VA	VA	5.00%	7/15/2029	18.3	4.670%	11/30/2010	AA	AA	Aa2	AA+	GENERAL OBLIGATION UNLTD	FED & ST TAX-EXEMPT	N
RICHMOND VA	VA	5.00%	7/15/2022	11.3	3.818%	12/22/2009	AA	AA	Aa2	AA	GENERAL OBLIGATION UNLTD	FED & ST TAX-EXEMPT	N
RICHMOND VA	VA	5.00%	7/15/2024	13.3	4.149%	12/22/2009	AA	AA	Aa2	AA	GENERAL OBLIGATION UNLTD	FED & ST TAX-EXEMPT	N



## VII. Appendix – Bond Pricing Comparables

### Selection of Comparable Capital Bonds based on recent transactions (cont.)

Name	State	Coupon	Maturity Date	Years to Maturity	Yield to Maturity	Issue Date	Ratings				Issue Type	Tax Provision	Insured
							Composite	S&P	Moody	Fitch			
TRENTON N J	NJ	3.00%	7/15/2012	1.3	0.706%	6/15/2010	NA	NA	Aa2	NA	GENERAL OBLIGATION UNLTD	FED & ST TAX-EXEMPT	N
TRENTON N J	NJ	4.00%	7/15/2013	2.3	1.032%	6/15/2010	NA	NA	Aa2	NA	GENERAL OBLIGATION UNLTD	FED & ST TAX-EXEMPT	N
TRENTON N J	NJ	4.00%	7/15/2014	3.3	1.417%	6/15/2010	NA	NA	Aa2	NA	GENERAL OBLIGATION UNLTD	FED & ST TAX-EXEMPT	N
ST PAUL MINN INDPT SCH DIST NO	MN	3.00%	2/1/2017	5.9	2.367%	10/1/2010	AA+	AAA	Aa2	NA	GENERAL OBLIGATION UNLTD	FED & ST TAX-EXEMPT	N
ST PAUL MINN CAP IMPT	MN	2.00%	9/1/2015	4.5	1.747%	3/11/2010	AA+	AAA	Aa1	NA	GENERAL OBLIGATION UNLTD	FED & ST TAX-EXEMPT	N
ST PAUL MINN PORT AUTH REV	MN	3.00%	12/1/2011	0.7	0.885%	12/1/2010	NA	NA	A1	NA	REVENUE BONDS	FED BQ/ST TAX-EXEMPT	N
ST PAUL MINN PORT AUTH REV	MN	3.00%	12/1/2012	1.7	1.080%	12/1/2010	NA	NA	A1	NA	REVENUE BONDS	FED BQ/ST TAX-EXEMPT	N
ST PAUL MINN PORT AUTH REV	MN	3.00%	12/1/2013	2.7	1.404%	12/1/2010	NA	NA	A1	NA	REVENUE BONDS	FED BQ/ST TAX-EXEMPT	N
ST PAUL MINN PORT AUTH REV	MN	4.38%	12/1/2024	13.7	4.020%	12/1/2010	NA	NA	A1	NA	REVENUE BONDS	FED BQ/ST TAX-EXEMPT	N
ST PAUL MINN PORT AUTH REV	MN	5.00%	12/1/2029	18.7	4.416%	12/1/2010	NA	NA	A1	NA	REVENUE BONDS	FED BQ/ST TAX-EXEMPT	N
ST PAUL MINN CAP IMPT	MN	2.00%	10/1/2012	1.5	0.742%	10/1/2010	AA+	AAA	Aa1	NA	GENERAL OBLIGATION UNLTD	FED & ST TAX-EXEMPT	N
ST PAUL MINN CAP IMPT	MN	2.50%	4/1/2017	6.0	2.162%	10/1/2010	AA+	AAA	Aa1	NA	GENERAL OBLIGATION UNLTD	FED & ST TAX-EXEMPT	N
ST PAUL MINN CAP IMPT	MN	3.00%	10/1/2011	0.5	0.463%	10/1/2010	AA+	AAA	Aa1	NA	GENERAL OBLIGATION UNLTD	FED & ST TAX-EXEMPT	N
INDIANAPOLIS IND THERMAL	IN	3.00%	10/1/2012	1.5	1.410%	10/28/2010	A	A	A2	NA	REVENUE BONDS	FED & ST TAX-EXEMPT	N
INDIANAPOLIS-MARION CNTY IND P	IN	3.50%	7/1/2015	4.3	1.615%	4/6/2010	NA	NA	Aa1	NA	GENERAL OBLIGATION UNLTD	FED BQ/ST TAX-EXEMPT	N
INDIANAPOLIS-MARION CNTY IND P	IN	4.00%	1/1/2019	7.8	2.525%	4/6/2010	NA	NA	Aa1	NA	GENERAL OBLIGATION UNLTD	FED BQ/ST TAX-EXEMPT	N
ANNA POLIS MD	MD	2.50%	6/1/2012	1.2	0.586%	6/15/2009	AA+	AA	Aa1	AAA	GENERAL OBLIGATION UNLTD	FED BQ/ST TAX-EXEMPT	N
ANNA POLIS MD	MD	2.50%	6/1/2013	2.2	0.842%	6/15/2009	AA+	AA	Aa1	AAA	GENERAL OBLIGATION UNLTD	FED BQ/ST TAX-EXEMPT	N
ANNA POLIS MD	MD	3.25%	6/1/2019	8.2	2.642%	6/15/2009	AA+	AA	Aa1	AAA	GENERAL OBLIGATION UNLTD	FED BQ/ST TAX-EXEMPT	N
ANNA POLIS MD	MD	4.00%	6/1/2022	11.2	3.333%	6/15/2009	AA+	AA	Aa1	AAA	GENERAL OBLIGATION UNLTD	FED BQ/ST TAX-EXEMPT	N
ANNA POLIS MD	MD	4.00%	6/1/2023	12.2	3.533%	6/15/2009	AA+	AA	Aa1	AAA	GENERAL OBLIGATION UNLTD	FED BQ/ST TAX-EXEMPT	N
ANNA POLIS MD	MD	4.25%	6/1/2028	17.2	4.017%	6/15/2009	AA+	AA	Aa1	AAA	GENERAL OBLIGATION UNLTD	FED BQ/ST TAX-EXEMPT	N
ANNA POLIS MD	MD	4.25%	6/1/2029	18.2	4.055%	6/15/2009	AA+	AA	Aa1	AAA	GENERAL OBLIGATION UNLTD	FED BQ/ST TAX-EXEMPT	N
ANNA POLIS MD	MD	4.00%	6/1/2026	15.2	3.923%	6/15/2009	AA+	AA	Aa1	AAA	GENERAL OBLIGATION UNLTD	FED BQ/ST TAX-EXEMPT	N
ANNA POLIS MD	MD	3.50%	6/1/2017	9.2	2.164%	6/15/2009	AA+	AA	Aa1	AAA	GENERAL OBLIGATION UNLTD	FED BQ/ST TAX-EXEMPT	N

## VII. Appendix – State Funding Detail

### 2007 – 2011 State Funding Sources

#### State Funding Sources<sup>1</sup>

(\$s in Millions)	2007 Actual	2008 Actual	2009 Actual	2010 Actual	2011 Adopted
<b>General Fund:</b>					
Pension System Subsidy	\$ 2.88	\$ 2.59	\$ 2.51	\$ 2.65	\$ 1.55
Capital Fire Protection	1.27	1.25	1.00	0.99	0.99
PILOTs	0.48	0.43	0.42	0.41	0.43
<b>Total General Fund</b>	<b>4.64</b>	<b>4.27</b>	<b>3.93</b>	<b>4.04</b>	<b>2.97</b>
<b>State Grants</b>					
State Grants Fund	1.65	1.98	(0.03)	0.91	-
State Liquid Fuels Fund	0.87	0.96	0.93	0.89	0.89
Sanitation Fund	0.10	0.14	0.14	0.13	0.13
<b>Total State Grants</b>	<b>2.62</b>	<b>3.08</b>	<b>1.04</b>	<b>1.92</b>	<b>1.02</b>
<b>Total State Funding</b>	<b>\$ 7.26</b>	<b>\$ 7.36</b>	<b>\$ 4.98</b>	<b>\$ 5.97</b>	<b>\$ 3.98</b>

Sources: a. Data from City Controller's Office

Notes: 1. Excludes amounts for utilities of State owned properties