

## STATUS REPORT

TO: Dauphin County Board of County Commissioners ("Commissioners")

FROM: Department of Community and Economic Development ("DCED") and Act 47 Coordinator Team ("Act 47 Team")

RE: City of Harrisburg ("City") Act 47

DATE: March 9, 2011

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The Commissioners have requested DCED and the Act 47 Team to provide a status report to them on March 9, 2011, in connection with the City's Act 47 matter, which follows.

1. On December 15, 2010, a determination of municipal financial distress was ordered by DCED Secretary Austin Burke pursuant to the Municipalities Financial Recovery Act, 53 P.S. § 11701.101, *et seq.*, ("the Act") to the City.

2. On or about January 12, 2011, DCED Secretary Burke appointed the Harrisburg Act 47 Coordinator Team, which includes The Novak Consulting Group, the Pennsylvania Economy League, O'Donnell Associates and Stevens & Lee law firm.

3. The Act 47 Team has "targeted" June 1, 2011, as the approximate date to file its Act 47 Plan ("Plan").

4. Since its appointment in January 2011, the Act 47 Team has performed extensive document review and analysis, has conducted numerous personal interviews, and continues that work.

5. On February 9, 2011 the Act 47 Team and DCED officials met with the Commissioners in executive session to discuss the County litigation in the Court of Common Pleas of Dauphin County.

6. On February 14, 2011, the Act 47 Team issued a "cost containment letter" to the City requesting the City to perform the following (see attached copy of letter):

- (i) Freeze spending for discretionary purchases
- (ii) Freeze hiring and impose overtime restrictions
- (iii) Prepare contingency plans
- (iv) Limit capital project expenditures
- (v) Review grant and third party funds

- (vi) Maintain flexibility to exercise all available strategies to minimize expenditures and accelerate revenue flows

7. On March 2, the Act 47 Team issued a second spending directive based on a further analysis of the City's cash flow. The directive acknowledged the positive response of the City to the February 14 letter and provided further guidance in dealing with potential cash flow shortfalls over the next several months so as to avoid an adverse impact on health and safety within the City. (See attached copy of letter.)

8. On February 23, 2011, DCED petitioned the Dauphin County Court of Common Pleas for intervenor status in cases involving TD Bank, M&T Bank and Assured Guaranty Municipal. The City's request for continuance of the hearing scheduled for March 1, 2011, was granted by Judge Hoover on February 24, 2011, so that the City could retain new counsel for the case. The Judge said he would set a new date for the hearing. DCED requested that the hearing not be scheduled before June 1 in order to allow the Act 47 process to proceed. The Judge took under advisement the City's motion to dismiss and/or stay the proceedings.

9. On February 28 and March 7, the Act 47 Team held public meetings in the Harrisburg community to (1) receive public comment from citizens and (2) explain the Act 47 process. The meetings were not held to present solutions or results or to make recommendations.

10. DCED officials and/or the Act 47 Team have met with: (1) the Mayor and City Administrative staff; (2) City Council President; (3) City Council in a public meeting; (4) the County Commissioners; (5) multiple stakeholders, both public and private; (6) Assured Guaranty Municipal; (7) AMBAC; (8) Lambdastar, Inc.; (9) Covanta; and (10) the City's Cravath lawyers. DCED officials and the Act 47 Team are working in multiple areas, including but not limited to the following areas concerning Debt:

- The Harrisburg Authority Debt
- The Parking Authority Debt
- City Debt

The Act 47 Team has reviewed the City's outstanding general obligation debt, including loans and leases; debt obligations guaranteed by the City, primarily the Resource Recovery Facility (RRF); and other obligations of component units of the City. The Act 47 Team reviewed (i) the City's audited financial statements; (ii) the Harrisburg Authority's financial statements; (iii) the Harrisburg Parking Authority's audited financial statements; (iv) various offering documents of bond transactions; (v) closing documents, including indentures and guarantee agreements, for the various outstanding financing transactions; (vi) the DCED filings for the various outstanding debt transactions; and (vii) other debt summaries of outstanding debt transactions compiled by various other interested parties, including the financial advisor of the Harrisburg Authority. Based on the analysis of all relevant information received to date and described above, the Act 47 Team is confident that all debt and other financing obligations have been identified and accounted for and a true financial analysis can be completed.

The City's preliminary 2011 cash flow analysis that has been prepared by the Pennsylvania Economy League ("PEL") indicates that the City has a structural annual deficit of at least \$4 million dollars. The \$4 million structural deficit includes all of the City's current general obligation debt requirements, including capital leases.

In fiscal year 2011, the City's guaranteed debt obligations for all of the RRF debt and swap agreements equal approximately \$18,898,000 over the course of the year. Assuming that cash flows from the incinerator would provide only \$5 million available for debt obligations, the City's current guarantee agreements would obligate the City to pay approximately \$13.9 million of RRF debt and swap obligations in fiscal year 2011. Adding the guaranteed amounts not covered by the Harrisburg Authority's cash flows available for debt obligations to the City's current structural deficit would increase the City's total deficit at the end of fiscal year 2011 to approximately \$18.9 million. The amount of cash available for debt service from the incinerator is estimated to be \$5 million in fiscal year 2011. This amount and potential future cash flow projections are yet to be verified subject to receipt and review of certain Harrisburg Authority documents by the Act 47 Team. Below is a summary of the current RRF debt and swap obligations due in fiscal year 2011:

<u>Date</u>	<u>Debt / Swap Obligation</u>	<u>Guarantor(s)</u>	<u>Amount Due</u>
1/1/2011	Covanta Loan	City	637,500
3/1/2011	1998 Bonds	City	279,125
3/1/2011	2003 A Bonds	City	647,263
3/1/2011	2003 B Bonds	City	290,850
3/1/2011	2003 C Bonds	City	607,125
4/1/2011	Covanta Loan	City	637,500
5/1/2011	2002 A Notes	City	402,688
6/1/2011	2003 D-1 Bonds	City & County	826,350
6/1/2011	2003 D-2 Bonds	City & County	1,625,000
6/1/2011	2003 E Bonds	City & County	289,729
6/1/2011	2003 F Bonds	City	283,245
6/1/2011	2003 D Swap - Cap	City & County	284,616
6/1/2011	2003 D Swaps	City & County	576,587
6/1/2011	County's PNC Note	County	350,000
7/1/2011	Covanta Loan	City	637,500
9/1/2011	1998 Bonds	City	279,125
9/1/2011	2003 A Bonds	City	647,263
9/1/2011	2003 B Bonds	City	290,850
9/1/2011	2003 C Bonds	City	607,125

<u>Date</u>	<u>Debt / Swap Obligation</u>	<u>Guarantor(s)</u>	<u>Amount Due</u>
10/1/2011	Covanta Loan	City	812,722
11/1/2011	2002 A Notes	City	1,242,688
12/1/2011	2003 D-1 Bonds	City & County	826,350
12/1/2011	2003 D-2 Bonds	City & County	1,625,000
12/1/2011	2003 E Bonds	City & County	1,809,729
12/1/2011	2003 F Bonds	City	1,748,245
12/1/2011	2003 D Swap - Cap	City & County	284,616
12/1/2011	2003 D Swaps	City & County	0
12/1/2011	County's PNC Note	County	350,000
			<u>18,898,791</u>

Based on the City's cash flow projections for fiscal year 2011, the City will not be able to meet any of its current obligations with respect to the guarantee agreements for any of the RRF debt or swap obligations.

DCED and the Act 47 Team understands the severity of the current situation with respect to the RRF debt and how it impacts not only the City and the County of Dauphin, but also other municipalities in the region and ultimately the Commonwealth of Pennsylvania. Based on discussions with several market participants, including rating agency analysts, the market's view of the City is as an interconnected operation including the enterprise funds and the RRF.

The City has received several proposals in response to the RRF debt situation, including such alternatives as sale of assets, lease of City facilities, and ultimately bankruptcy. The Act 47 Team is committed to continue its efforts to evaluate all options with respect to the RRF debt situation, as well as the City structural deficit. The ultimate goal of the Act 47 Team is to evaluate and provide independent analyses and recommendations to move the City and ultimately the County and other interested parties toward a common solution.

In addition to the review of Debt discussed above, the Act 47 Team and DCED continue to review and analyze the following for recommendations in the Plan:

- Revenue
- Workforce
  - Workforce and Collective Bargaining
  - Pensions and Other Post-Employment Benefits
- Elected and Executive Officials
  - Mayor's Office and City Council
- Financial Management
  - Finance Department

- Information Technology
- Capital Improvement Plan
- Other Professional Services
  - Human Resources
  - Insurance and Risk Management
  - Human Relations
  - Law
- Public Safety
  - Fire
  - Police
- Public Works
  - Department of Public Works
  - Public Authorities
- Community and Economic Development
  - Community Development
  - Housing
  - Economic Development
  - Code Enforcement
- Taxation
- Litigation
- Intermunicipal Cooperation opportunities
- Grants/Incentives

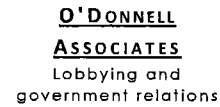
11. DCED and the Act 47 Team will review the City's circumstances with and without a Chapter 9 bankruptcy analysis.

12. DCED and the Act 47 Team will look at the City's circumstances with and without a sale/lease of assets analysis.

13. DCED and the Act 47 Team are performing the above work with no preconceived conclusions.

DCED and the Act 47 Team will be pleased to discuss the above information with the Commissioners at their convenience.

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February 14, 2011

The Honorable Linda Thompson  
Mayor of the City of Harrisburg  
Dr. Martin Luther King, Jr. Government Center  
10 North 2nd Street  
Harrisburg, Pennsylvania 17101

The Honorable Gloria Martin-Roberts  
President of Council  
Dr. Martin Luther King, Jr. Government Center  
10 North 2<sup>nd</sup> Street  
Harrisburg, Pennsylvania 17101

Mayor Thompson and Council President Roberts:

The Act 47 Team appreciates the efforts that you, your colleagues and appointees have made to assist us in the initial phases of the Act 47 process. We have begun preliminary cash flow analysis, and based on the initial review, we believe it appropriate to offer a series of recommendations in advance of the full plan. Preliminary analysis indicate that the City's expenditures will outpace revenue collection as early as March of 2011. At that time a transfer from any available surplus fund into the General Fund will be necessary to meet current operational and City debt obligations until sufficient tax receipts are received by the City.

Because of the very delicate nature of the City's immediate financial picture, it is critical that all expenditures be carefully scrutinized prior to obligating the City for payment. We understand that the City has been forced to carefully examine and curtail expenditures during the past year, and we would ask that your staff be directed to continue this practice in 2011. Only expenditures that are essential to the health, safety and welfare of City residents should be approved.

It is necessary to mitigate any shortfall in FY2011 and limit any additional liabilities that the City would have to address in addition to implementing a Recovery Plan. In our role as Act 47 Recovery Plan Coordinator, we request that the City undertake the following steps commensurate with the financial crisis it faces:

- **Spending freeze for discretionary purchases:** The City should eliminate FY2011 discretionary purchases of certain categories of material and equipment, such as computers, peripherals, and printers, as well as office supplies until current inventories are depleted. Equipment or vehicle purchases should also be deferred except in urgent cases. Optional contracts for professional services or commodities should be reduced or eliminated whenever possible. Finance Director approval should be required for all discretionary purchases over \$2,500.

- **Hiring freeze and overtime restrictions:** Finance Director approval should be required for any exceptions to a general hiring freeze, including filling temporary, seasonal or paid intern positions in the FY2011 budget. Advance Finance Director approval of overtime should be required, although we understand unforeseeable events may occur, particularly for public safety departments. Bureau Directors should work closely with the Finance Director to monitor and manage overtime throughout the year.
- **Prepare contingency plans:** Each Department/Office or Bureau should prepare financial contingency plans for the rest of the year showing budgeted spending levels and an alternative "spending reduction" scenario that incorporates the steps recommended in this memo
- **Limit capital project expenditures:** The City should review capital spending on non-emergency projects. Critical, non-emergency priorities should be identified and funded if they cannot be deferred. The remainder of funds should be set aside for contingencies.
- **Review grant and third party funds:** The City should review discretionary grant-funded or third-party supported programs that require cash or in-kind matches from the City's General Fund to determine whether they should be temporarily suspended.
- **Maintain flexibility to exercise all available strategies:** We urge the Mayor and City Council to avoid taking actions that may preclude the implementation of various work force, operational, or budgetary strategies in the future. This includes any investments by the City or its Authorities in technology or personnel that could limit opportunities for joint working, consolidation or other efficiency measures. As the preparation of the Recovery Plan is just beginning, limiting the scope of options available at this time would be detrimental to the City's long-term fiscal health.

Although expenditure items are of great concern as noted above, we would also suggest that management be diligent on revenue related matters to insure that all tax collection and utility billing activities are timely and appropriate follow up actions are taken to maximize the collection of revenues.

Please note that our recommendations contemplate cases where essential service delivery, grant recovery, or net revenue generation benefits may justify exceptions. Please contact me or Gerry Cross from our team if you have specific questions about such exceptions. We understand that the steps we are urging you to take are drastic, but it is our view that they are commensurate with the seriousness of the City's fiscal distress. It is imperative for the Administration and City Council to take every possible step to reduce expenditures and monitor its cash flow needs very closely throughout 2011.

Thank you for your continued cooperation as we work together to restore fiscal stability to the City of Harrisburg.

Sincerely,



Julia D. Novak, President  
The Novak Consulting Group  
Act 47 Coordinator

*City of Harrisburg, Act 47*

cc: Daniel C. Miller, City Controller  
City Councilmembers  
Beth Gabler, City Clerk  
Bob Krobath, Director, Bureau of Financial Management  
Fred Reddig, Executive Director, Governor's Center for Local Government Services  
Gerald Cross, PA Economy League  
Robert O'Donnell

The Novak  
Consulting Group



O'DONNELL  
ASSOCIATES  
Lobbying and  
government relations

March 2, 2011

The Honorable Linda Thompson  
Mayor of the City of Harrisburg  
Dr. Martin Luther King, Jr. Government Center  
10 North 2nd Street  
Harrisburg, Pennsylvania 17101

The Honorable Gloria Martin-Roberts  
President of Council  
Dr. Martin Luther King, Jr. Government Center  
10 North 2<sup>nd</sup> Street  
Harrisburg, Pennsylvania 17101

Mayor Thompson and Council President Roberts:

The Act 47 Team appreciates the positive response from the City with regards to our February 14 spending directive. We recognize that there are certain positions that must be filled and expenses that must be committed in order for the City to operate effectively. We will be supportive of prudent and intentional decisions in that regard.

During the development of the Act 47 Plan, we examine past cash flow trends and prepare cash flow projections by month for 2011. We recently reviewed these cash flow projections with the City Administration and we noted the possibility -- particularly if the timing of both expected real estate revenue and necessary debt payments do not coincide to the City's advantage -- that the City could encounter a cash shortage in March 2011. In the event that this timing might cause a temporary shortfall in cash, we recommend that the City be prepared to cover any shortage with an interfund loan from the City's Workers Compensation Fund. This use of a fund balance for temporary use is possible and we are confident that such a use is appropriate from the standpoint of Commonwealth requirements for funding the City's Workers Compensation Fund. We are aware that the City has tried to curtail interfund borrowing, which is a prudent practice, but this transfer may be necessary to meet anticipated expenditures. Nonetheless, this practice should occur sparingly and only when necessary to ensure continued operations of a municipality. Since the City is operating this year without the cash margin normally provided by a Tax Anticipation Note, the alternate use of funds can be appropriate in this circumstance. In addition, any transfer that might occur needs to be treated appropriately under the City's accounting system as a loan or "due to/due from" entry for specific accounts. Should a transfer be necessary, specific payback terms would be necessary to ensure that the transfer is repaid by a date certain, for example end of May or June after receipt of most of the City's real estate taxes. These specific procedures will allow the City use of the funds without the possible negative consequences that would otherwise accompany the temporary use of funds for specific purposes. Because this transfer cannot be implemented without several weeks of notice and approvals, it is prudent for the City to shortly begin this cash transfer process so that funds are available if needed.

Please contact me or Gerald Cross from our team if you have any questions about this directive.

Thank you for your continued cooperation.

Sincerely,

A handwritten signature in black ink, appearing to read "Julia D. Novak". The signature is fluid and cursive, with the first name "Julia" and last name "Novak" clearly distinguishable.

Julia D. Novak, President  
The Novak Consulting Group  
Act 47 Coordinator

cc: Daniel C. Miller, City Controller  
City Councilmembers  
Beth Gabler, City Clerk  
Bob Kroboth, Director, Bureau of Financial Management  
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Gerald Cross, PA Economy League  
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