

Frequently Asked Questions:

A Proposed City of Detroit Consent Agreement and Public Act 4 Of 2011

Why is the city of Detroit being offered a consent agreement?

The state of Michigan, under the authority of Public Act 4 of 2011, began a financial review of the city's finances in early 2012. This financial review occurs when a city appears to be headed towards a fiscal crisis. This review can lead to several outcomes including a signed consent agreement or installation of an emergency manager. At this time, the state is offering the city a consent agreement.

» What is Public Act 4 of 2011?

Public Act 4 of 2011 is known as the Local Government and School District Fiscal Accountability Act. This act is designed to provide the state with tools to oversee the fiscal affairs of local governments and school districts. In Michigan, there is a balancing act that must be weighed addressing the fiscal affairs of local government. Home rule is a concept that means a local government, particularly a city, has the right to self-determination of its own affairs.

» What is the PA 4 of 2011 process?

PA 4 is a three-step process. The first step, if certain triggers are hit, calls for the state to begin a preliminary review. The preliminary financial review is completed by the Michigan Department of Treasury and is generally done in about 30 days. This review will determine whether or not a potential financial crisis exists. If a potential crisis is deemed to exist, the next step calls for the state to appoint a financial review team. This team will assess if a financial crisis exists and what type of solution may be possible. The financial review team may find:

- ▶ no financial crisis exists
- ▶ a financial crisis exists, but a consent agreement has been worked out or an Emergency Manager must be appointed

» What is the basis for the potential emergency or crisis for Detroit?

The review team has found that the city of Detroit has run a deficit every year since 2005. Furthermore, the review team has found that the city is nearing a cash crisis and is expected to be out of money in May 2012.

» Why was the financial review team sued?

The review team was sued in Ingham County Circuit Court for violating the Open Meetings Act. This act states that public bodies must meet in public in an open and transparent manner. Traditionally, it was thought that financial review teams could meet in private. However, an Ingham County judge has ruled that the Detroit financial review team must meet in public. The review team has done so since the ruling.

» Who are the members of the financial review team?

The financial review team is charged with assessing a city's financial situation and determining whether or not an emergency crisis exists. The members of the review team in Detroit include state treasurer Andy Dillon, Michigan Department of Treasury senior policy advisor Brom Stibitz; department of treasury local government services bureau director

Fredrick Headen; Irvin Reid, retired President of Wayne State University; Glenda Price, former President of MaryGrove College; Conrad Mallett, President of the Detroit Medical Center; Jack Martin, CPA from Martin, Arrington, Desai and Meyers; Isaiah McKinnon, retired Detroit Police Chief; Doug Ringler, state director of the Office of Internal Audits; and Shirley Stancato, president of New Detroit. The financial review team will propose and vote on a consent agreement to be presented to the city of Detroit.

» **What is a consent agreement?**

A consent agreement is a contract between a local government and the state of Michigan. This agreement states that a local government will undertake certain actions to address a fiscal emergency or crisis. The state will provide oversight in this agreement. Each consent agreement may have a different structure.

» **Do all consent agreements have similar provisions?**

All consent agreements have several common factors. These include:

- ▶ regular financial reporting
- ▶ authority of state treasurer to place a local government in receivership for breach of consent agreement

» **Who approves the consent agreement?**

A consent agreement is brought forward by the financial review team. The process may differ slightly, but ultimately the city council must approve it. Once the consent agreement has been signed by the financial review team and the city council, the Governor has final approval to execute the agreement.

» **Are there optional provisions in a consent agreement?**

A consent agreement may include:

- ▶ a grant to the mayor, city council, finance director or other officers powers similar to the emergency manager
- ▶ a local government under a consent agreement does not have a duty to bargain with collective bargaining units
- ▶ may require retention of consultants or auditors
- ▶ may utilize state financial management and technical assistance

- ▶ may require a recovery plan or continuing operations plan

» **What is the basic consent agreement being offered to the city of Detroit?**

The consent agreement basically outlines a process by which the city must undertake certain actions and meet certain financial and operating benchmarks to avoid a fiscal crisis. As part of this process, the state and the city will appoint members of a financial advisory board to oversee the restructuring and will play an important role in the city’s finances.

» **What is a financial advisory board?**

A financial advisory board is a group of individuals from various backgrounds who help ensure the city government is restructuring operations to maintain the city’s short- and long-term financial solvency.

» **Who will be on the Detroit financial advisory board?**

The Detroit financial advisory board will have nine members. Gov. Snyder will appoint one person, the state treasurer will serve on the board and will also appoint one member, Mayor Bing will appoint two persons and the Detroit City Council will appoint one person. The last three individuals will be selected from by the mayor and city council from a list of six provided by the Governor.

» **What are the qualifications for being on the board?**

Each member of the board must have at least 10 years of experience in restructuring, financial transactions and labor and pension issues.

» **Who determines if someone meets these qualifications?**

The Michigan Association of Certified Public Accountants will determine if appointees and perspective appointees meet the qualifications.

» **Is there anyone who cannot be a member?**

Yes. Current city government staff members or members of the city council may not be on the financial advisory board.

» **Do the financial advisory board members receive compensation?**

Yes. The state will pay each member of the board \$25,000 annually for his/her work, with the exception of the state treasurer, who receives no compensation.

» **What are the powers of the financial advisory board?**

The board may first adopt rules for its own operation. The board may hire and employ professional staff members or consultants to serve it. The board will have at its main function the overseeing of the city's restructuring plan. The board has the right to approve any city operating and capital budget to ensure consistency with the restructuring plan. The board has the authority to review and approve all of the city's capital market and debt transactions. The board will review and approve organizational changes to city government. The board will also appoint a chief operating officer, chief financial officer and human resources director. All of these positions are deemed necessary by the review team to ensure that the restructuring plan is being followed and implemented.

» **Who are the new appointed officials and what are their duties?**

The chief financial officer, chief operations officer and human resources director will be responsible for overseeing the operations and restructuring of city government. They will report to both the mayor and the financial advisory board.

» **Who appoints these three new officials?**

They will be appointed by the financial advisory board with recommendations from the Governor and the Detroit mayor.

» **Does the proposed consent agreement remove all power from the mayor and city council?**

No. The mayor and city council retain their powers to some extent. They will be able to pass ordinances and resolutions and continue to run the city on a day-to-day basis. The financial advisory board will have the power to oversee and drive the budget process. The mayor and the city council also play a limited role in selecting financial advisory board members and appointed officials.

» **The consent agreement talks about a restructuring plan. What is this plan and who came up with it?**

Public act 4 of 2011 allows for several types of financial and restructuring plans to address city fiscal crisis situations. The two types of plans are a continuing operations plan and a recovery plan. A continuing operations plan is a financial plan to ensure the short- and long-run fiscal solvency of a city government. The plan must include a detailed revenue and spending estimate, ensure reasonable maintenance of capital infrastructure, an operating plan, cash flow projections and an evaluation of pension and other post employment benefit obligation costs. The plan may include other elements as deemed necessary. A recovery plan and continuing operations plan are similar in scope. The main difference is that a continuing operations plan is put forward by local government officials while the recovery plan is developed by the state treasurer. The recovery plan will include many of the same elements as a continuing operations plan along with procedures for cash control, quarterly reporting by the local government to the state; the recovery plan will supersede any locally passed budget. The Detroit consent agreement includes a recovery plan developed by the financial review team.

» **What does the consent agreement propose to do to alleviate Detroit's fiscal crisis?**

The consent agreement proposes a recovery plan that was developed by the financial review team. The implementation of this plan will be overseen by the financial advisory board. Components of the proposal include:

- ▶ Reduction in the number of employees
- ▶ Outsourcing of certain government functions
- ▶ Reduction in the number of vendors to the city
- ▶ Tax amnesties and changes to the tax structure of the city
- ▶ Better management of city's real estate
- ▶ Any other plans a needed
- ▶ Best practices related to health care benefits
- ▶ Potential sale of city assets

The state of Michigan considers these actions as necessary to begin to reduce the city's short-term fiscal stress and begin the process of reaching long-term solutions for city fiscal stress. There are no guarantees

that these actions will work. Only full implementation over the course of time will tell if they are enough to alleviate the fiscal crisis.

» Under the consent agreement can the mayor or the financial advisory board cancel or modify union contracts?

No. While the city does not have to bargain with labor units, the city or the financial advisory board must abide by existing terms and may not cancel or modify existing agreements.

» Does the city have to bargain with labor units?

No. The city does not have to bargain with labor units while the consent agreement is in place. If the city does attempt to come to an agreement with labor units, these agreements will be subject to approval by the financial advisory council.

» What are the main differences between the city's proposed consent agreement and state agreement?

In the city's proposal, the mayor and council would retain power. The mayor would have the power to appoint the chief operating, human resources director and the chief financial officer. The financial advisory board would have limited power. Note the difference in this comparison of the different sections of the proposal. In particular, the words "review and approve" in the state-proposed consent agreement are replaced by "review and comment" in a number of sections. These wording differences appear in the sections on contracts, judgment levies, and organizational changes, and most importantly, in the budget section.

» What would be the relationship between the financial advisory board and the city?

The financial advisory board would appoint a liaison officer who would work with the mayor on the restructuring plans. The liaison officer would be paid by the board and would have limited powers.

» Would the membership of the board in the city's proposal be the same as the state proposal?

No. The board makeup would be determined by a different set of criteria. The state treasurer would be an

automatic member. Beyond that, the Governor would receive only one appointment. The mayor would be allowed to appoint two members and city council would be allowed to appoint two members. The council would have to pick members from a list of six provided by the Governor. Finally, the council would be able to appoint one person of its choosing, independent of the Governor.

» Would the criteria for board membership remain the same?

No, there are changes to the criteria for board membership. The criteria would be five years instead of ten years in restructuring, pensions and or a financial background.

» Would the city be responsible for the cost of the board under its proposal?

No, the state treasury would be responsible for paying the cost of the financial advisory board.

» When would the financial emergency be over in the city's proposal?

The emergency would end when the city's general fund had not run a deficit for three consecutive years and the city's general obligation debt was rated in one of the four highest debt rating categories that are available via the rating agencies.

» Why is the Governor referring to New York City in 1975 as a model?

In 1975, New York City faced a major fiscal crisis and was very close to filing for bankruptcy. This bankruptcy filing was avoided via state and federal fiscal assistance. With such assistance, the state of New York required the city to be under an emergency financial control board. The board, similar to the financial advisory board proposed for Detroit, oversaw the city's fiscal affairs, budgeting, collective bargaining and debt issuance. The New York City mayor and city council were still in charge of the city overall. This structure was considered very successful and helped New York City become fiscally solvent in the 1980's and beyond.

» What Happened to New York City in 1975?

New York City was on the verge of bankruptcy in 1975. The city had run out of cash and the banks were unwilling to lend any further short term financing to the

city government. The city was losing population and jobs and faced a major fiscal crisis.

» **What were the main options available to New York City?**

There were four major options presented to city leaders. The first option would be increasing taxes, which would require legislative approval. The second option was state and federal aid. The last two options were oriented to budget reductions and retrenchment. One of these options was to reduce services in general and focus only on core city services. The second option was a general cut in spending across services areas, which would include wage freezes and layoffs. These options are not dissimilar to some of the options facing the city of Detroit in 2012.

» **Can't Detroit raise taxes to address its problems?**

The city of Detroit has fewer revenue options than New York City then or now. This is because Michigan law is very different from New York state law. Detroit's revenue options are limited without state policy changes.

» **What did the state of New York initially do?**

Initially, the state of New York established a municipal assistance corporation (MAC). The purpose of the MAC was to provide a conduit through which the city could issue new debt, but have that debt backed by another entity. This strategy only worked temporarily. Eventually, it became clear that this strategy alone would not be enough to convince the banking or investment community to keep the city afloat.

» **What was the New York City Emergency Financial Control Board?**

It became clear in 1975 that the MAC was not working. The financial emergency law, passed by the New York Legislature in 1975, laid out the conditions for providing a new policy tool to address the crisis. The major tool created was the emergency financial control board (EFCB). The board was made up of seven members. This included the Governor of New York, the state comptroller, the mayor and city comptroller, who were all ex officio members. Three of the board members were from the private sector. These were from the highest levels of the business community. All of these board members brought significant resources

from their own expertise and their organizations. At its peak, the board comprised 24 members, including lawyers, political scientists, policy experts and public management experts. The cost of this staff was \$500,000 and was shared between the city and the state.

» **What did the EFCB do to address the crisis?**

New York City was allowed to create a financial recovery plan. This plan then had to be approved by the EFCB. There were several plans presented

» **What happened to New York City employees?**

In 1974, the city of New York had the most expansive government of any U.S. city and it included universities, a hospital, health department and a school district. Further, the city must protect many unique institutions such as the United Nations headquarters. Between 1974 and 1977, the city of New York laid off more than 60,000 employees.

» **What was the financial plan developed to address New York City's crisis?**

As stated by the New York law, the plan had several preconditions. First, the city had to operate with a balanced budget by FY 1978. The EFCB also was empowered to set revenue estimates. The city was required to follow these revenue estimates in preparing its budget. At first, several financial plans were developed. The plan that was finally accepted by the board included state and federal aid, as well as major service reductions and spending cuts.

» **What were the EFCB's powers?**

The EFCB had several tools to address the fiscal crisis. The first was that all city funds were deposited in the EFCB account. The EFCB then gave the city funds as were needed. The second tool was the ability to remove any elected or appointed official who did not follow the board's orders. These tools were never used. Besides these powers, other powers and authority were made available to EFCB. One of those powers was the oversight and approval of all city contracts. Another was the installation of a deputy state comptroller oversee the city's book. These powers combined allowed the city to begin accessing the credit markets again.

The EFCB had the right to reject any bargaining agreements. The state of New York also imposed a wage freeze and no increase in benefit costs over the period of the fiscal emergency. While protecting overall collective bargaining rights, the city and EFCB managed to lead to a major slowdown in labor costs during the crisis.

» **What were the EFCB’s limitations or restrictions?**

There were important limitations on the EFCB. The first was that the board could not dictate the type of spending in which the city could engage, it had to stay at an aggregate policy level. The other major limitations related to information flows and administrative constraints. The EFCB’s small staff (in contrast to the size of the city) made it difficult from them to accomplish their work. Further, they had no real access to information or data other than what the city made available to them. These were real concerns that made the board’s work difficult. Finally, the press and citizen groups made it difficult for the board to work at times. Constant scrutiny and claims of mismanagement would continue to haunt the board throughout its service.

» **Was the EFCB successful?**

While it is always difficult to understand cause and effect exactly in these situations, in broad strokes the EFCB process did seem to work. New York City finances did make a major recovery. However, part of the reasons for that recovery was that New York’s diversified and international corporate base responded well during the economic change of the last 30 years. Tax revenues grew tremendously placing much less fiscal stress on the city over time.

» **What happened to the EFCB?**

After the crisis was over, the EFCB was renamed the Financial Control Board (FCB) and it has remained in place, though its role is now not nearly as important and it has much more limited powers related to monitoring the city’s fiscal situation. The FCB was to expire in 2008 but is now in effect until 2033 with renewed legislation.

» **When did New York City’s bonds achieve investment grade status?**

In 1983, nearly eight years after the crisis, New York City earned investment grade rating from the federal

government and the rating agencies. Today, New York City bonds all have investment grade ratings.

» **Why was former Washington D.C. Mayor Anthony Williams brought in to testify about the consent agreement?**

Washington D.C. faced a major fiscal crisis in 1995 due to revenue limitations, costly pensions and a population decline. The U.S. Congress, which oversees the District of Columbia, imposed a financial control board on the city in return for fiscal relief. The board could reject or approve the city budget, review and reject all future contracts and debt issuance. In general, this approach has been considered successful and played a role in the fiscal revitalization of the District of Columbia.

» **Have any other major U.S. cities faced similar crises?**

Yes. The city of Philadelphia faced a fiscal crisis in 1991 after five years of accumulating nearly \$1 billion in deficits. The banks were unwilling to lend further to support the city government. The state of Pennsylvania created the Pennsylvania Intergovernmental Cooperation Authority. The authority was designed to help Philadelphia regain financial stability. The most important power the authority has is to review and approve the city’s annual budget and its required five-year financial plan. Philadelphia has had a substantial fiscal recovery, though the current recession has been difficult. The authority remains in place today.

» **What if the city of Detroit fails to abide by the consent agreement?**

If the mayor or city council attempts to sue the state or challenge the constitutionality of the agreement or the PA 4 law, the agreement will be considered null and void and either an emergency manager will be appointed or bankruptcy proceedings will begin. If the city fails to abide by the consent agreement and is in “material breach,” the state can immediately appoint an emergency manager.

» **How will we know, under the consent agreement terms, when the financial crisis is over?**

Under the consent agreement, there are two possible pathways for an end to the crisis. The first would be that the city would have no year-end deficit in any

fund, no structural imbalance between revenues and spending and for three consecutive years or the state treasurer determines that no crisis exists under the conditions of existing laws. Such a completion shall be called a period of financial stability. There is a caveat that the financial advisory board may vote to continue to be in existence until such time as it determines there is no need for the board.

» What are the powers of an emergency manager?

This is a listing of the basic powers that an emergency manager has under the law. As stated previously, a consent agreement may provide for these same powers to a city itself, such as the mayor or city council, except for the power to modify or terminate collective bargaining agreements.

- ▶ Analyze factors that led to a financial crisis
- ▶ Amend, revise and approve or disprove a city budget
- ▶ Receive and disburse all state and federal grants
- ▶ Require and approve or disapprove any outstanding obligations
- ▶ Require special financial or operational reports from city staff
- ▶ Examine all books and records
- ▶ Make, approve, disapprove any appropriation, contract or expenditure of the local government
- ▶ Review payroll
- ▶ Reject, modify or terminate the contract provisions
- ▶ Reject, modify or terminate collective bargaining agreements on a temporary basis
- ▶ If underfunded, take control of a local pension system
- ▶ Consolidate, eliminate or transfer government departments and functions
- ▶ Employ consultants and staff as needed
- ▶ May initiate court proceedings to ensure orders are followed
- ▶ Authorize borrowing and engage in talks with creditors
- ▶ Enter into agreements with other governments for cooperation or consolidation
- ▶ With approval of Governor, seek disincorporation or dissolution of a city
- ▶ Exercise power to adopt and amend resolutions and ordinances
- ▶ Replace and remove any appointed officials, commission or authority members

» Are there any checks and balances on the emergency manager?

The emergency manager (EM) serves at the pleasure of the Governor. He or she may be removed at any time if the Governor feels that the EM is not performing to his satisfaction. The EM may not: a) sell or transfer city assets, b) modify or terminate collective bargaining agreements, c) disincorporate or dissolve a municipality without approval of the Governor. Further, an EM may not raise taxes without a vote and consent of the people of the jurisdiction.

The citizens of the city in question do not have any direct recourse to appeal the decisions of the emergency manager. Citizens may direct questions or concerns to their state representative, state senator or to the Governor. Many EMs host town hall meetings or other public events to keep the public informed of what actions they are taking and obtain input on possible course of action.

» What Happens to the Detroit consent agreement if PA 4 of 2011 is suspended by the petition drive?

The consent agreement provides the possibility of the suspension of Public Act 4 of 2011 via a citizen referendum. If the citizen referendum is approved by the state board of canvassers, Public Act 4 of 2011 will be suspended. In this case, the consent agreement states that it will be authorized under Michigan law Act 7 of 1967, also known as the Urban Cooperation Act. Thus, it is possible that the consent agreement would still be in effect even if Public act 4 of 2011 is suspended. However, it should be noted that this is a novel legal strategy and may be subject to court review.

» Many opponents of the consent agreement state that cities should have the right to determine their own affairs. What is the basis for this argument?

Michigan has legal provisions for cities to operate under what is known as “home rule”. Home rule is a notion that city governments should have the right to determine their own affairs. This would include passing laws and regulations to protect the health and welfare of their citizens. Home rule does not give a city free reign; the city must abide and not contravene all applicable state and federal laws. Opponents of the

PA 4 of 2011 cite that the law takes away home rule from city government. Proponents of the law believe that this temporary withdrawal of some home rule powers is necessary for the fiscal crisis to be addressed.

» What does the Michigan Constitution say about city home rule?

In the Michigan Constitution (Article VII, Sec. 22), cities and city residents have the right to adopt a charter. A charter is a form of local constitution that allows a city to determine how it will organize its affairs. This provision also gives cities the right to pass ordinances and resolutions, which are a form of local government law. The city charter and local ordinances must not contravene state law or interfere with other localities.

» Does Michigan have a city home rule act?

The Michigan Legislature passed a law in 1909 (Act 279) which is known as the Home Rule City Act. This act provides for the incorporation of cities, allows cities to collect taxes and fees, enter into debt agreements and pass city charters. The act requires a city charter to contain certain provisions, including

elections, duties of city officials, a budget process, provisions for protecting public health and safety and a process for adopting city ordinances and resolutions.

» What are the options for organizing city government under home rule?

Michigan cities have options in approaching home rule. A city may form a government that is a city manager form of government or a so-called strong mayor form of government. A strong mayor form of government means that the mayor is chief executive who has certain powers such as hiring and firing of certain government officials and the presentation of a budget plan. In this setting, the mayor is head of the executive branch of government. The city of Detroit operates with a strong mayor form of government.

A second option is the weak mayor-city manager form of government. The city manager becomes the city’s chief executive officer who may have certain powers as allowed by the city charter or city council. The city council is the legislative body that passes local ordinances or resolutions. In this setting, the mayor is a member of the legislative body and has no executive powers. Most Michigan cities operate with a city manager form of government.

For More Information

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