



STATE OF MICHIGAN  
DEPARTMENT OF TREASURY  
LANSING

RICK SNYDER  
GOVERNOR

ANDY DILLON  
STATE TREASURER

**DATE:** March 26, 2012

**TO:** Governor Snyder

**FROM:** Detroit Financial Review Team:  
Andy Dillon  
Frederick Headen  
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**SUBJECT:** Report of the Detroit Financial Review Team

On January 10th, 17th, 19th, 24th, and 31st; February 28th; and March 13th, 21st, and 26th 2012, Detroit Financial Review Team members met and reviewed information relevant to the financial condition of the City. Based upon those reviews, the Review Team concludes, in accordance with Section 13(4)(c) of Public Act 4 of 2011, the Local Government and School District Fiscal Accountability Act, that the City of Detroit is in a condition of severe financial stress as provided in Section 14 of the Act, and that a consent agreement has not been adopted pursuant to Section 13(1)(c) of the Act.

## I. Background

### A. Preliminary Review

On December 6th through December 21st, 2011, the Department of Treasury conducted a preliminary review of the finances of the City of Detroit to determine whether or not probable financial stress existed. Section 12(1) of the Act provides that a preliminary review may be conducted if one or more of the conditions enumerated therein occurs. The preliminary review of the City of Detroit resulted from the conditions enumerated in subdivisions (j), (m), (o), (q) and (r) of Section 12(1) having occurred within the City.<sup>1</sup>

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<sup>1</sup> Subsection (j) provides that “[t]he local government has violated a requirement of sections 17 to 20 of the uniform budgeting and accounting act, 1968 PA 2, MCL 141.437 to 141.440. Subsection (m) provides that “[a] local government is in breach of its obligations under a deficit elimination plan or an agreement entered into pursuant to a deficit elimination plan.” Subsection (o) provides that “[a] municipal government has ended a fiscal year in a deficit condition.” Subsection (q) provides that “[a] local government has been assigned a long-term debt rating within or below the BBB category or its equivalent by 1 or more nationally recognized credit rating agencies.” Subsection (r) provides that

The preliminary review found, or confirmed, the following:

- The City had violated requirements of Public Act 2 of 1968, the Uniform Budgeting and Accounting Act. Section 17 of the Act provides that “[t]he legislative body of the local unit shall amend the general appropriations act as soon as it becomes apparent that a deviation from the original general appropriations act is necessary and the amount of the deviation can be determined.”<sup>2</sup>

For example, for the year ending June 30, 2010, the human resources apprentice training program exceeded its budget by over \$2.3 million, the insurance premium line item exceeded its budget by over \$12 million, and the police operations line item exceeded its budget by \$15.8 million. Consequently, the general fund had line items that exceeded budgeted amounts, in the aggregate, by almost \$58 million. Unaudited 2011 figures indicated that line items amounting to \$97 million exceeded their budget, including an excess of \$25 million for fire and \$44 million for police.

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“[t]he existence of other facts or circumstances that in the state treasurer’s sole discretion for a municipal government are indicative of municipal financial stress.”

<sup>2</sup> The Review Team was advised by a member of the City Council that the implication of the preliminary review (i.e., that the City Council had failed to amend budgets to prevent over expenditures) was incorrect in that the City Council is not authorized to initiate budget amendments. The point made by the City Councilmember is well taken.

Section 17 of Public Act 2 of 1968, the Uniform Budgeting and Accounting Act, reads, in part, as follows:

(1) Except as otherwise provided in section 19, a deviation from the original general appropriations act shall not be made without amending the general appropriations act. Subject to section 16(2), the legislative body of the local unit shall amend the general appropriations act as soon as it becomes apparent that a deviation from the original general appropriations act is necessary and the amount of the deviation can be determined. An amendment shall indicate each intended alteration in the purpose of each appropriation item affected by the amendment. The legislative body may require that the chief administrative officer or fiscal officer provide it with periodic reports on the financial condition of the local unit.

(2) If, during a fiscal year, it appears to the chief administrative officer or to the legislative body that the actual and probable revenues from taxes and other sources in a fund are less than the estimated revenues, including an available surplus upon which appropriations from the fund were based and the proceeds from bonds or other obligations issued under the fiscal stabilization act, 1981 PA 80, MCL 141.1001 to 141.1011, or the balance of the principal of these bonds or other obligations, *the chief administrative officer or fiscal officer shall present to the legislative body recommendations which, if adopted, would prevent expenditures from exceeding available revenues for that current fiscal year.* Emphasis supplied.

We would read the obligation of a legislative body to amend a budget under subsection (1) of Section 17 of the Act to apply only upon receipt of a recommendation from the chief administrative officer or fiscal officer pursuant to subsection (2) of the Act.

- City officials had not filed an adequate or approved deficit elimination plan with the Department of Treasury for the 2010 fiscal year. On December 20, 2010, City officials filed an audit report that reflected a \$155 million cumulative deficit in the general fund, a \$1.4 million cumulative deficit in the airport fund, and a \$3.5 million cumulative deficit in the local street fund. As of December 2011, City officials had not filed a plan that would reduce the general fund deficit. In fact, new data estimated the general fund's deficit increasing to \$196 million for 2011. The deficits in the airport and local street funds were eliminated in 2011.

There had been deficits in the general fund exceeding \$100 million dating back to 2005. These deficits had fluctuated between over \$155 million and over \$300 million. One of the primary methods the City had used to reduce the deficits had been to issue more debt. Total general fund debt, and other long term liability proceeds for the years between 2005 and 2010, was over \$600 million, temporarily reducing the deficits by an equal amount. Debt proceeds reduce the deficit in the year the debt is issued, but reduce fund balance over time as debt service payments increase.

General Fund (Unrestricted) Deficits and Debt Proceeds

Year	Deficit	Debt Proceeds
2005	(\$155,404,035)	\$248,440,183
2006	(\$173,678,707)	\$34,892,659
2007	(\$155,575,800)	--
2008	(\$219,158,138)	\$75,210,007
2009	(\$331,925,012)	--
2010	(\$155,692,159)	\$251,663,225
2011	(\$196,577,910)	--

- The City's deficit elimination plans and proposed budgets proved to be unrealistic. City officials either had been incapable or unwilling to manage the finances of the City. For example, the 2008 fiscal year deficit elimination plan reported \$58 million in expenditure reductions in the general fund and \$69 million (excluding debt proceeds and revenue sharing) in revenue enhancements for 2010. However, the 2010 general fund balance ended in a deficit condition of over \$155 million and would have been much greater if not for \$250 million in new debt. Again, the 2009 deficit elimination plan certified in November of 2010 projected a 2011 surplus while the actual fund balance for the general fund ended with a deficit estimated at close to \$200 million.

City officials had promised restructuring and consolidation, including hiring freezes and improved tax collection. Finally in mid-2011, City officials submitted a deficit elimination plan for the 2010 deficit which included revenue initiatives of over \$200 million and expenditure reductions of over \$300 million, most of which were to take place in future periods and were questionable, such \$10 million from selling Windsor tunnel rights and \$50 million in improved income tax collections. One version of the deficit elimination plan estimated that the City would

be able to realize an additional \$154 million annually from collecting income taxes from residents who work outside the City. Projected expenditure reductions relied heavily upon union concessions which had not historically materialized.

- The City had a mounting debt problem. In 2010, annual debt service requirements exceeded \$597 million. As of June of 2011, the long-term debt of the City exceeded \$8 billion, excluding unfunded actuarial pension, other postemployment benefit liabilities, and discretely presented component units such as the library and downtown development authority. However, if one included the unfunded actuarial pension liability of \$615 million (offset by an almost \$1.4 billion pension asset) and the other postemployment benefit liability of over \$4.9 billion, the City's total long-term liabilities were more than \$12 billion. (See table below.) The latter amount did not include substantial sums of interest which were over \$4.9 billion. In comparison, if one took the total long-term debt of the City compared to total net assets, the City would have had for 2010 a debt to net assets ratio of 32.64 to 1.

	General Obligations	Revenue Bonds	Pension Obligation Certificates	Other
Governmental	\$1,033,233,278	\$125,520,622	\$1,194,003,260	\$284,276,052
Sewage		\$2,894,198,302	\$90,114,924	\$15,046,961
Transportation	\$6,271,722		\$105,143,913	\$28,238,095
Water		\$2,159,831,662	\$79,517,902	\$25,979,109
Automobile		\$11,341,382		\$10,225,829
Other				\$162,187
Unallocable				
	<u>\$1,039,505,000</u>	<u>\$5,190,891,968</u>	<u>\$1,468,799,999</u>	<u>\$363,928,233</u>
	Other Post Employ- ment Benefits	Pension Liability	Pension Asset*	Total
Governmental				\$2,637,033,212
Sewage				\$2,999,360,187
Transportation				\$139,653,730
Water				\$2,265,328,673
Automobile				\$21,567,211
Other				\$162,187
<u>Unallocable</u>	<u>\$4,982,355,243</u>	<u>\$615,701,032</u>	<u>(\$1,371,848,955)</u>	<u>\$4,226,207,320</u>
Total	\$4,982,355,243	\$615,701,032	(\$1,371,848,955)	\$12,289,312,520

\*Pension asset may already be factored into actuarially determined pension liability

- Prior to 2008, in order to obtain better interest rates and reduce debt related costs, the City entered into interest rate swaps and swap options (i.e., where two or more parties enter into an agreement to exchange interest cash flows). Exchanging, or “swapping,” a variable interest rate for a fixed rate would have benefited the City had market interest rates increased. However, rates subsequently decreased, impacting the City negatively. Because the fall in interest rates was not predicted, ramifications of increased annual payments resulted. In addition to principal and interest payments, the City must pay amounts called “hedging derivatives”, which over the life of the debt is an additional \$1,136,007,248.

The preliminary review found the City to be at risk of a termination event which would occur if the City’s credit rating were downgraded below Baa3 or its equivalent. On January 8, 2009, such an event occurred. However, the City avoided the immediate demand for payment by entering into another agreement which allocated wagering tax revenues to a trust to be used as collateral for future payments thus reducing the benefits of those cash flows to the City. New termination events included the failure to maintain a certain level of funds in the trust, further downgrades in the City’s credit rating, or appointment of an emergency manager.

As stated by the City’s auditors, “[s]hould such Termination Events occur in connection with the Swap Agreements, and not be cured, there presently exists significant risk in connection with the City’s ability to meet the cash demands under the terms of the amended Swap Agreements.” According to estimates, if an “event” occurred, the City would face a \$280 million to \$400 million termination payment. According to the preliminary review, City officials intended to sell water and sewer bonds to unwind a portion of the swaps. The notional amount, or face value, of these outstanding hedging derivatives in 2011 was over \$3.8 billion and had a market value of (\$560 million).

- The City’s long-term bond rating fell below the BBB category and is considered “junk”, speculative, or highly speculative. According to a Thomson Reuters June 24, 2011 article, “Fitch downgraded the rating on about \$453 million of Detroit’s unlimited-tax general obligation bonds to BB-minus from BB-plus, and dropped the rating on the City’s approximately \$486 million of limited-tax GO bonds to B-plus from BB. The rating on about \$1.5 billion of pension bonds was cut to BB-minus from BB-plus. The lower unlimited-tax general obligation rating from Fitch matches the Ba3 rating with a negative outlook from Moody’s Investors Service. Standard & Poor’s Ratings Services rates Detroit’s GO bonds BB with a stable outlook.”
- Not only did the City have large external debts, but it also had large debts owed to itself in the form of inter-fund loans. As of June 30, 2010, the City had inter-fund balances amounting to over \$447 million and unaudited 2011 balances of \$334 million. Concurrently, the City had operating surpluses in its general fund for most of the more recent fiscal years. However, the general fund incurred substantial deficits because of the subsidies it paid to other funds, such as \$72 million to the transportation fund. However, most of the outgoing transfers \$133 million

were made for debt service and pension funds. The total amount transferred from the general fund according to 2011 draft figures was \$215 million.

- The City experienced significant cash-flow shortages. In 2010, the City received \$250 million in fiscal stabilization bond proceeds. The City also received \$55 million in delinquent property tax receipts from Wayne County and \$20 million from a DTE Energy escrow account. However, despite these inflows of substantial amounts of cash, City officials were projecting a cash shortage.

Based upon projections made available by the City at the time of preliminary review, the general fund had a forecasted ending cash balance of \$115.5 million as of October 28, 2011. However, the actual cash balance as of that date was \$96.1 million, an overestimation of \$19.4 million. The City revised its cash forecast based on a series of new assumptions which projected that the City would experience a cash shortage starting in April 2012, of \$1.6 million and would end its fiscal year in June 2012 with a cash shortage of \$44.1 million absent remedial action.

- The City experienced difficulty making its required payments to its pension systems. Years of exceptional pension benefits had increased costs to the City. The preliminary review found that current police and fire employees enjoy multipliers of 2.5 percent for 25 years of service and 2.1 percent thereafter.<sup>3</sup> However, a newer one-year agreement was approved to limit to 2.1 percent the multiplier for earnings after September 2011. General employees (i.e., non-police and fire) had negotiated a tiered system of 1.6 percent for the first 10 years, 1.8 percent for the next 10 years, 2.0 percent for the next five years, and 2.2 percent for any remaining years.

In June of 2005, City officials issued \$1.44 billion of pension obligation certificates to fund the City's two retirement systems with a renegotiated payment schedule of 30 years. More recently, City officials contemplated not making required payments to pension systems as a cost-savings measure. However, subsequent negotiations with representatives of the pension systems resulted in a "smoothing" that allowed City officials to make five years of pension payments over a seven-year period. Annual required payments reflected in the 2011 fiscal year financial audit, excluding debt payments related to the certificates, was \$110 million, an increase of \$41 million from the 2010 fiscal year.

- There were questionable balances in the 2010 audit report of the City's pension systems. The auditors were unable to obtain sufficient evidence supporting approximately \$216 million of the retirement systems' alternative investments.

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<sup>3</sup> Multipliers are used in calculating retirement pay in defined benefit plans. For example, for an employee with 30 years of service who was making \$50,000 at retirement, a 2.5 percent multiplier would yield \$37,500 in annual retirement benefits ( $0.025 \times 30 \times \$50,000$ ). By comparison, a 1.5 percent multiplier would yield an annual retirement benefit of \$22,500, a difference of \$15,000 annually.

- The financial audit report for the 2010 fiscal year indicated that the City's poor financial management impacted the City's administration of various federal grant programs and posed potential threats to the City's continued receipt of such grants. The audit report cited numerous findings and offered the following examples of questioned and potentially disallowed costs:
  - Nutrition for Women, Infants and Children (approximately \$1.0 million in questioned costs in addition to accounting, eligibility and fund reconciliation issues).
  - Community Development Block Grant (approximately \$12.7 million in questioned salary costs).
  - HOME, a home investment partnership program, (approximately \$846,000 in salary costs; \$273,000 in questioned indirect planning costs).

Based upon the foregoing preliminary review, the State Treasurer concluded, and reported to the Governor on December 21, 2011, that probable financial stress existed in the City of Detroit and recommended the appointment of a financial review team.

## B. Review Team Findings

On December 27, 2011, the Governor appointed a ten-member Financial Review Team. The Review Team convened on January 10th, 17th, 19th, 24th, and 31st; February 28th; and March 13th, 21st, and 26th 2012.

### 1. Conditions Indicative of a Financial Emergency

The Review Team found, or confirmed, the existence of the following conditions based upon information provided by City officials, or the City's audit firm, or other relevant sources:

- According to the City's fiscal year 2011 financial audit, the cumulative general fund deficit increased by 62.5 percent, from \$91,094,688 as of June 30, 2010 to \$148,071,674 as of June 30, 2011. While the general fund had an operating surplus (i.e., revenues in excess of expenditures) of \$150,077,184, net transfers out of the general fund of \$206,947,605 resulted in a negative net change in the general fund balance of \$56,870,421.
- Financial audit reports for the City for its last nine fiscal years reflect significant variances between general fund revenues and expenditures, as initially budgeted and as amended, versus general fund revenues and expenditures actually realized. These variances, which are depicted on the next two pages, are reflective of the practice of which the Review Team was informed, of City officials adopting budgets that knowingly overestimated revenues. However, the overestimates of revenue largely were offset by corresponding overestimates in general fund expenditures.

General Fund (Amended) Budget to Actual Variances  
Fiscal Years 2003-11

	<u><b>2002-03</b></u>	<u><b>%</b></u>	<u><b>2003-04</b></u>	<u><b>%</b></u>	<u><b>2004-05</b></u>	<u><b>%</b></u>
<u><b>Revenues</b></u>						
Budgeted	\$1,411,438,181		\$1,491,324,664		\$1,411,559,555	
Amended	\$1,455,091,091		\$1,557,611,152		\$1,573,240,100	
Actual	<u>\$1,379,940,668</u>		<u>\$1,375,067,276</u>		<u>\$1,357,023,161</u>	
Variance	(\$75,150,423)	(5.16)	(\$ 182,543,876)	(11.71)	(\$ 216,216,939)	(13.74)

<u><b>Expenditures</b></u>						
Budgeted	\$1,500,934,902		\$1,645,328,307		\$1,486,784,830	
Amended	\$1,603,280,231		\$1,849,483,383		\$1,733,451,270	
Actual	<u>\$1,463,658,564</u>		<u>\$1,577,561,963</u>		<u>\$1,492,451,332</u>	
Variance	\$ 139,621,667	8.71	\$ 271,921,420	14.70	\$ 240,999,938	13.90

	<u><b>2005-06</b></u>	<u><b>%</b></u>	<u><b>2006-07</b></u>	<u><b>%</b></u>	<u><b>2007-08</b></u>	<u><b>%</b></u>
<u><b>Revenues</b></u>						
Budgeted	\$1,446,899,263		\$1,460,450,319		\$1,511,369,289	
Amended	\$1,716,282,293		\$1,685,082,568		\$1,711,079,894	
Actual	<u>\$1,400,871,987</u>		<u>\$1,487,435,488</u>		<u>\$1,303,429,698</u>	
Variance	(\$315,410,306)	(18.37)	(\$ 197,647,080)	(11.73)	(\$ 407,650,196)	(23.82)

<u><b>Expenditures</b></u>						
Budgeted	\$1,484,834,179		\$1,466,705,687		\$1,580,231,599	
Amended	\$1,631,152,256		\$1,702,154,178		\$1,696,476,581	
Actual	<u>\$1,410,081,217</u>		<u>\$1,278,109,169</u>		<u>\$1,181,358,285</u>	
Variance	\$ 221,071,039	13.55	\$ 424,045,009	24.91	\$ 515,118,296	30.36



General Fund (Amended) Budget to Actual Variances  
Fiscal Years 2003-11  
(Continued)

	<u>2008-09</u>	<u>%</u>	<u>2009-10</u>	<u>%</u>	<u>2010-11</u>	<u>%</u>
<u>Revenues</u>						
Budgeted	\$1,424,125,131		\$1,651,938,137		\$1,361,741,809	
Amended	\$1,755,335,605		\$1,695,653,435		\$1,650,138,387	
Actual	<u>\$1,268,371,151</u>		<u>\$1,187,977,093</u>		<u>\$1,220,258,093</u>	
Variance	(\$ 486,964,454)	(27.74)	(\$ 507,676,342)	(29.93)	(\$ 429,880,294)	(26.05)
<u>Expenditures</u>						
Budgeted	\$1,557,486,518		\$1,644,170,276		\$1,374,762,769	
Amended	\$1,798,321,382		\$1,834,191,680		\$1,558,893,986	
Actual	<u>\$1,155,896,702</u>		<u>\$1,068,938,078</u>		<u>\$1,070,180,909</u>	
Variance	\$ 642,424,680	35.72	\$ 765,253,602	41.72	\$ 448,713,077	31.35

- The general fund of the City has not experienced a positive year-end fund balance since the 2004 fiscal year, when the year end balance was \$69,216,269. (See Table 1.) Beginning with the 2005 fiscal year, the general fund has had a negative year-end balance that has ranged from \$33,594,434 for the 2005 fiscal year to 266,733,641 for the 2009 fiscal year. During a number of these years, general fund revenues actually exceeded general fund expenditures. However, there were sizable transfers out of the general fund to support other City operations, such as transportation, that resulted in negative year end balances in the general fund.
- The City has experienced, and continues to experience, a significant depletion of its cash.<sup>4</sup> Early in 2012, City officials had estimated that the City would deplete its cash by spring and have a negative cash balance of \$44.0 million by June 30, 2012. In an effort to address this situation,

<sup>4</sup> Confirmation by the Review team of the City's ongoing cash shortages is consistent with the conclusion reached by other financial assessments. For example, the report of the Mayor's Crisis Turnaround Team, that was commissioned by the current City administration, noted the following:

The City is critically short of cash as a result of a \$280 million estimated accumulated deficit and a growing structural deficit in the current fiscal year as projected revenues decline. The new administration must act quickly to realize substantial improvements in selected revenues and cost categories in the \$2.1 billion General City Agency Budget. The [Crisis Turnaround] team recommends that the new administration establish a financial recovery strategy based on the projected deficit

City officials had proposed adjustments to collective bargaining agreements projected to save \$102.0 million for fiscal year 2012 and \$258.0 million for fiscal year 2013. However, the tentative collective bargaining agreements negotiated to date are projected to yield, at best, savings of only \$47.0 million and \$172.0 million for fiscal years 2012 and 2013, respectively.

- On March 20, 2012, Moody's Investor Service downgraded approximately \$2.5 billion of the City's existing debt, some of it to five to six levels below investment grade. Among the reasons cited by Moody's Investor Service for the downgrade were the City's "weakened financial position, as evidenced by its narrow cash position, its reliance upon debt financing, and ongoing negotiations with its labor unions regarding contract concessions." On March 22, 2012, Fitch Ratings also downgraded approximately \$2.5 billion of the City's existing debt for substantially similar reasons.

## 2. Review Team Meetings

At its initial meeting on January 10, 2012, the Review Team met with Joseph A. Kowalski of the certified public accounting firm KPMG.

On January 17, 2012, Review Team members conducted a series of meetings in the City of Detroit with Dave Bing, Mayor; Kirk Lewis, Chief of Staff; Chris Brown, Chief Operating Officer; Charles Pugh, City Council President; Gary Brown, City Council President Pro Tem; Ralph Godbee, Jr., Police Chief; Donald Austin, Fire Commissioner; Cheryl Johnson, Finance Director and City Treasurer; Alfred Jordan, Group Executive, Utilities; Ed McNeil, Special Assistant to the President of AFSCME, Council 25; and John Mack, Assistant to Ed McNeil.

On January 19, 2012, Review Team members conducted a series of meetings in the City of Detroit with Patrick Aquart, Human Resources Director; Joseph Martinico, Labor Relations Director; Karla Henderson, Group Executive, Planning and Facilities; Charles Dodd, Information Technology Services Director; Pamela Scales, Budget Director; Linda Bade, City Assessor; Joseph Duncan, President, Detroit Police Officers Association; James Moore, Vice-President, Detroit Police Command Officers Association; Junetta Wynn, President, Detroit Police Lieutenants and Sergeants Association; Daniel F. McNamara, President, Detroit Fire Fighters Association; Jeffrey Pegg, Vice President, Detroit Fire Fighters Association; Teresa Sanderfer, Secretary, Detroit Fire Fighters Association; and Robert Shinske, Treasurer, Detroit Fire Fighters Association.

On January 24, 2012, Review Team members conducted a series of meetings in the City of Detroit with Dave Bing, Mayor; Kirk Lewis, Chief of Staff; Chris Brown, Chief Operating Officer; Gaurav Malhotra, of the certified public accounting firm Ernst & Young; Charles Pugh, City Council

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for the 2010-2011 fiscal year and repayment of ad hoc funding actions. This would require a target of \$250 million to \$300 million in ongoing annual revenue increases and cost savings.

President; Gary Brown, City Council President Pro Tem; Andre Spivey, Councilmember; and Joe Harris, Former City of Detroit Auditor General.

On January 31, 2012, Review Team members conducted a series of meetings in the City of Detroit with Kenneth V. Cockrel, Jr., Councilmember; Robert Anderson, Planning and Development Director; George Jackson, Jr., President and Chief Executive Officer, Detroit Economic Growth Corporation; Brian Holdwick, Executive Vice President, Detroit Economic Growth Corporation; Waymon Guillebeaux, Executive Vice President, Detroit Economic Growth Corporation; and Glenn Long, Vice President and Chief Operating Officer, Detroit Economic Growth Corporation; James Tate, Councilmember; Saunteel Jenkins, Councilmember; Brenda Jones, Councilmember; Irvin Corley, City Council Fiscal Analyst; Jerry Pokorski, City Council Financial Analyst; and Deputy City Treasurer Mike Bridges.

The Review Team also conducted public meetings in the City on February 28th, and March 13th, 21st, and 26th. At these public meetings, the Review Team received public comment and considered the options afforded to the Review Team by statute.

### C. Conclusion

Based upon the foregoing information, meetings and review, the Review Team confirms the findings of the preliminary review, concludes in accordance with Section 13(4)(c) of Public Act 4 of 2011, the Local Government and School District Fiscal Accountability Act, that the City of Detroit is in a condition of severe financial stress as provided in Section 14 of the Act, and that a consent agreement has not been adopted pursuant to Section 13(1)(c) of the Act.

## II. Section 13(3) Requirements

Section 13(3) of the Act requires that this report include the existence or an indication of the likely occurrence of any of the conditions set forth in subdivisions (a) through (l).<sup>5</sup> The conditions in subdivisions (e), (f), and (g) of Section 13(3) exist or are likely to occur, as follows:

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<sup>5</sup> Subdivisions (a) through (l) of Section 13(3) of the Act provide as follows:

- (a) A default in the payment of principal or interest upon bonded obligations, notes, or other municipal securities for which no funds or insufficient funds are on hand and, if required, segregated in a special trust fund.
- (b) Failure for a period of 30 days or more beyond the due date to transfer 1 or more of the following to the appropriate agency:
  - (i) Taxes withheld on the income of employees.
  - (ii) For a municipal government, taxes collected by the municipal government as agent for another governmental unit, school district, or other entity or taxing authority.

- The City had a general fund deficit of \$148,071,674 as of June 30, 2011, which was not eliminated within the two-year period preceding the end of the fiscal year of the City during which this Review Team report is received. (Section 13(3)(e)).
  - As of January 31, 2012, the City Council's Fiscal Analysis Division was projecting a general fund deficit of \$270.0 million for the current fiscal year ending June 30, 2012, which would exceed five percent of the \$1.2 billion budgeted revenues for the general fund. (Section 13(3)(f)).
  - As previously noted, City officials did not file an adequate or approvable deficit elimination plan with the Department of Treasury for the 2010 fiscal year. Nor did City officials do so for the 2011 fiscal year. Furthermore, past deficit elimination plans have proven to be unrealistic. For example, the 2009 fiscal year deficit elimination plan projected a 2011 fiscal year general fund surplus, but the general fund ended with an actual deficit of \$148,071,674. (Section 13(3)(g)).
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(iii) Any contribution required by a pension, retirement, or benefit plan.

(c) Failure for a period of 7 days or more after the scheduled date of payment to pay wages and salaries or other compensation owed to employees or benefits owed to retirees.

(d) The total amount of accounts payable for the current fiscal year, as determined by the state financial authority's uniform chart of accounts, is in excess of 10% of the total expenditures of the local government in that fiscal year.

(e) Failure to eliminate an existing deficit in any fund of the local government within the 2-year period preceding the end of the local government's fiscal year during which the review team report is received.

(f) Projection of a deficit in the general fund of the local government for the current fiscal year in excess of 5% of the budgeted revenues for the general fund.

(g) Failure to comply in all material respects with the terms of an approved deficit elimination plan or an agreement entered into pursuant to a deficit elimination plan.

(h) Existence of material loans to the general fund from other local government funds that are not regularly settled between the funds or that are increasing in scope.

(i) Existence after the close of the fiscal year of material recurring unbudgeted subsidies from the general fund to other major funds as defined under government accounting standards board principles.

(j) Existence of a structural operating deficit.

(k) Use of restricted revenues for purposes not authorized by law.

(l) Any other facts and circumstances indicative of local government financial stress or financial emergency.

Governor Snyder  
March 26, 2012  
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### III. Review Team Report Transmittal Requirements

Section 13(3) of the Act also requires that a copy of this report be transmitted to Mayor Dave Bing, Detroit City Councilmembers, the Speaker of the House of Representatives, and the Senate Majority Leader.

cc: Dave Bing, Mayor  
Detroit City Councilmembers  
James Bolger, Speaker of the House of Representatives  
Randy Richardville, Senate Majority Leader

**Table 1**  
**City of Detroit**  
**General Fund Revenues, Expenditures,**  
**And Change in Fund Balance**

	<u>2002-03</u>	<u>2003-04</u>	<u>2004-05</u>
Revenue	\$1, 379,940,668	\$1,375,067,276	\$1,357,023,161
Expenditures	\$ 1,463,658,564	\$1,577,561,963	\$1,492,451,332
Current Surplus/ (Deficit)	<u>(\$83,717,896)</u>	<u>(\$202,494,687)</u>	<u>(\$135,428,171)</u>
Other Financing Sources	(\$32, 790,755)	\$86,278,519	47,986,831
Net Change in Fund Balance	(\$52,758,651)	(\$77,966,168)	(487,441,340)
Beginning Fund Balance	<u>\$206,220,362</u>	<u>\$140,304,407</u>	<u>\$69,216,269</u>
Change in Inventories	(\$13,157,304)	\$6,878,030	(\$15,369,363)
Ending Fund Balance	<u>\$140,304,407</u>	<u>\$69,216,269</u>	<u>(\$33,594,434)</u>

	<u>2005-06</u>	<u>2006-07</u>	<u>2007-08</u>
Revenue	\$1,400,871,987	\$1,487,435,488	\$1,303,429,698
Expenditures	\$1,410,081,217	\$1,278,109,169	\$1,181,358,285
Current Surplus/ (Deficit)	<u>(\$9,209,230)</u>	<u>\$209,326,319</u>	<u>\$122,071,413</u>
Other Financing Sources	(\$54,277,434)	(\$194,233,601)	(\$175,016,228)
Net Change in Fund Balance	(\$63,486,664)	15,092,718	(\$52,944,815)
Beginning Fund Balance	<u>(\$33,594,434)</u>	<u>(\$107,176,088)</u>	<u>(\$91,406,096)</u>
Change in Inventories	(\$10,094,990)	\$677,274	\$2,665,757
Ending Fund Balance	<u>(\$107,176,088)</u>	<u>(\$91,406,096)</u>	<u>(\$141,685,154)</u>

**Table 1**  
**(Continued)**  
**City of Detroit**  
**General Fund Revenues, Expenditures,**  
**And Change in Fund Balance**

	<u>2008-09</u>	<u>2009-10</u>	<u>2010-11</u>
Revenues	\$1,268,371,151	\$1,187,977,093	1,220,258,093
Expenditures	\$1,155,896,702	\$1,068,938,078	1,070,180,909
Current Surplus/ (Deficit)	<u>\$112,474,449</u>	<u>\$119,039,015</u>	<u>\$150,077,184</u>
Other Financing Sources	(\$236,535,259)	(\$209,943,411)	(\$206,947,605)
Net Change in Fund Balance	(\$124,060,810)	\$178,349,536	(\$56,870,421)
Beginning Fund Balance	<u>(\$141,685,154)</u>	<u>(\$266,733,641)</u>	<u>(\$91,094,688)</u>
Change in Inventories	(\$987,677)	(\$2,710,583)	(\$106,565)
Ending Fund Balance	<u>(\$266,733,641)</u>	<u>(\$91,094,688)</u>	<u>(\$148,071,674)</u>

Source: City of Detroit Annual Financial Audits