

## Michigan's New Local Financial Emergency Law (P.A. 436 of 2012)

Dr. Eric Scorsone  
**Michigan State University  
Extension**

---

# THE DEBATE

# EM (Opponents)

---

- **Arguments Against:**
  - Law does not work; does not provide for fiscal stability
    - Flint and Ecorse in and out several times
  - Loss of Democracy; Voters have elected officials (home rule) taken from them

# EM (Proponents)

---

- Arguments For:
  - Law provides tools for Governor and State to prevent fiscal crisis
  - Fiscally distressed communities are not protecting citizens and threaten other communities

# Do We Still have a Problem?

---

- 50 out of 579 school districts facing red ink (deficit)
- 1/3 of cities and municipalities facing deficit
  - Many are facing year over year chronic deficits
  - 12 cities operating with close to zero cash

# Current EM Communities

---

- **School Districts**

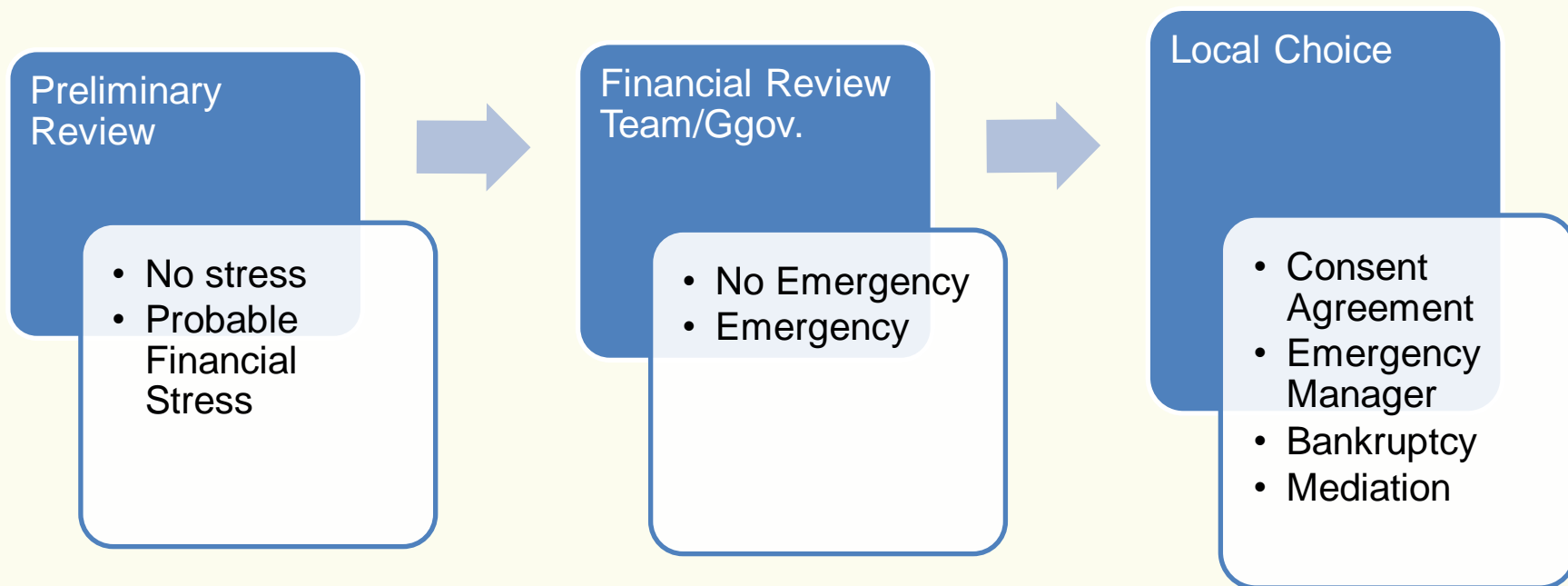
- Muskegon Heights, Highland Park, Detroit

- **Cities**

- Flint, Benton Harbor, Ecorse, Highland Park, Allen Park, Pontiac

- Inkster, River Rouge, Detroit

# P.A. 436 Process



---

# REVIEW PROCESS



# Preliminary Review Triggers

---

- Governing body or CAO requests
- Creditor (10k +)
- Elector petition
- Pension deposit missed
- Missed payroll
- Legislative resolution
- Violate revenue bond act
- Violate order of EFALB
- Violate budget law; Glenn Steill law
- Failure to file audit
- Failure to distribute taxes
- Failure to follow DEP
- Court ordered tax levy
- BBB or lower credit rating
- Other conditions
- School district failure to follow DEP

# Who is the Review Team?

---

- State Treasurer or designee  
(Superintendent or designee)
- Director of Dept. of Technology,  
Management and Budget or designee
- Nominee of Senate Majority Leader
- Nominee of Speaker of the House
- Governor may appoint other officials

# Review Team Powers

---

- Examine the books and records of local gov't
- Utilize the services of state agencies
- Negotiate and sign a consent agreement with CAO
- Must do their work with 60 days

# Review Team Fact Finding

---

- Report must indicate whether the following has or is likely to occur:
- Bond default
- Failure to transfer employee taxes, govt. taxes, pension funds,
- Missed payroll
- Excess accounts payable (+10%)
- Failure to eliminate existing deficit (2 yrs.)
- Projection of large deficit (5%+)
- Material loans between funds
- Use of restricted revenues
- Structural operating deficit
- Failure to comply with DEP
- Other facts

# Financial Emergency Definition

---

- 1 or more of previously reported facts exist or will exist soon
- Local govt. failed to comply with Review Team
- Local “govt. failed to comply with deficit elimination plan
- Chief Admin. Officer concludes that 1 or more factors exist or will exist soon

# Review Team Findings

---

- No Financial Emergency
- Financial Emergency
- Then the Governor comes into play....

# Governor's Decision

---

- Within 10 days , Governor must decide
- No Financial Emergency
- Financial Emergency

---

# **LOCAL GOVERNMENT CHOICES**



# Local Choices

---

- Consent Agreement
- Emergency Manager
- Bankruptcy filing (Ch. 9)
- Mediation/Neutral Evaluation

---

# **CONSENT AGREEMENT OPTION**

# Consent Agreement

---

- Local officials agree to operate under certain conditions but remain “in charge”
  - City of Detroit has Financial Stability Agreement
- Certain metrics must be met for consent agreement to end
- If consent agreement is not reached (30 days), Treasurer may require selection of another option

---

# **MEDIATION/NEUTRAL EVALUATION OPTION**

# Mediation/Neutral Evaluation

---

- Drawn from California local emergency finance law
- Local. Govt. and interested parties meet to attempt to come to agreement on obligations

# Mediation Process

---

- Local Govt. and interested parties select a mediator
- If local govt. selects option and fails to act in 7 days, Treasurer may require receivership
- Mediator has 60 days (+30 extra)

# Who is the Mediator?

---

- Training in conflict and dispute resolution
- 10 years of high level business or government experience
- In following areas: municipal finance, taxation, constitutional law, debt restructuring, bankruptcy, labor law

# Mediation Outcomes

---

- Settlement reached
  - But if Treasurer rejects, proceed to new option
- Settlement reached but requires Ch. 9
- Deadline passes with no resolution
- No response from interested parties
- Fiscal condition deteriorates
  - Pass resolution and recommend Ch. 9 to Governor



---

# **EMERGENCY MANAGER OPTION**

# What Happens First?

---

- Salaries, wages and accrual of benefits are suspended for all elected officials and CAO
- EM may restore that pay and benefits as they see fit

# Who are Emergency Managers?

---

- Minimum 5 years experience in finance, accounting or local/state budgets
- May be a resident of the local government
- Shall be an “individual”
  - In other words no ‘corporate’ persons
- Serves at the Pleasure of the governor
  - May be impeached by Legislature

# Emergency Managers Can:

---

- Analyze fiscal stress and take corrective actions
- Amend, review approve and disprove budgets
- Require, Amend, approve, disprove a plan to pay obligations
- Require special financial reporting
- Examine all records and accounts
- Make, approve and disprove any appropriation, contract, expenditure and loan

# Emergency Managers Can:

---

- Fill any vacancy
- Review payrolls or claims before payment
- Establish and implement staffing levels
- Reject or modify existing contracts
- Act as sole agent in collective bargaining
- If pension funding is below 80%, remove and appoint pension board members

# Emergency Managers Can:

---

- Consolidate or eliminate departments
- Engage in intergovernmental contracting
- Retain consultants
- Initiative legal action to enforce compliance
- Order a millage election
- Sell assets (subject to approval)

# Emergency Managers cannot or must:

---

- Cannot Raise taxes unilaterally
- Cannot Sell assets without Treasury approval
- Cannot violate city charter
- Must comply with state pension laws
- Must get State Financial Authority approval for contract termination, modification or rejection

# Collective Bargaining

---

- Agreement termination subject to state approval
- **Conditions:**
  - Must be reasonable and necessary
  - Must deal with a broad, generalized economic problem
  - Rejection or modification must be related to financial emergency
  - Cannot target specific employee classes



# Contract Clause

---

- U.S. Constitution (Article 1, Sec. 10, Clause 1)
- “No state shall....., pass any Law impairing the Obligation of Contracts”)
- Contract Clause was designed to prevent states from reliving persons or themselves of their debts

# But, U.S. Supreme Court..

---

- Under some conditions, states can impair contracts
- Leading cases
  - U.S. Trust Co. of NY vs. New Jersey
  - Stone vs. Mississippi

# Challenge to EM Actions

---

- Local Board can challenge certain EM actions
  - Asset sales, collective bargaining,
- LEFALB will determine if actions stands
  - Local board must propose equal alternative
  - Based on best interests of community

# EM Outcome

---

- Remove government from receivership  
or
- Appoint a receivership transition advisory board
  
- May also impose conditions:
  - Financial best practices
  - Financial training
  - Model city charter

# Receivership Transition Advisory Board (RTAB)

---

- Require a revenue consensus meeting
- Require monthly cash flow projections
- Review, amend and approve local budgets
- Review debt issuance requests
- Review collective bargaining
- Review deficit elimination plan
- Others.....

# Municipal Bankruptcy

---

- If EM believes no reasonable alternative exists.....
- With Governor approval, EM may apply for Ch. 9 Municipal Bankruptcy

---

# **MUNICIPAL BANKRUPTCY**

# Bankruptcy Approval

---

- Governor may deny request and force municipality to choose another option
- Court must ascertain that municipality meets criteria
  - Most importantly that they are or soon will be unable to pay upcoming obligations



# Muni Bankruptcy

---

- Similar to individual bankruptcy (debt adjustment)
- Judge has limited powers due to separation of powers
- May terminate contracts

# MB Outcome

---

- Plan of adjustment
- Interested parties and creditors receive a “haircut” less than they are owed
- Municipality or school district attains financial sustainability relative to obligations

- 
- **Thank you!**
  
  - **Dr. Eric Scorsone**
  - **Department of Agricultural, Food and Resource Economics**
  - **scorsone@msu.edu**