

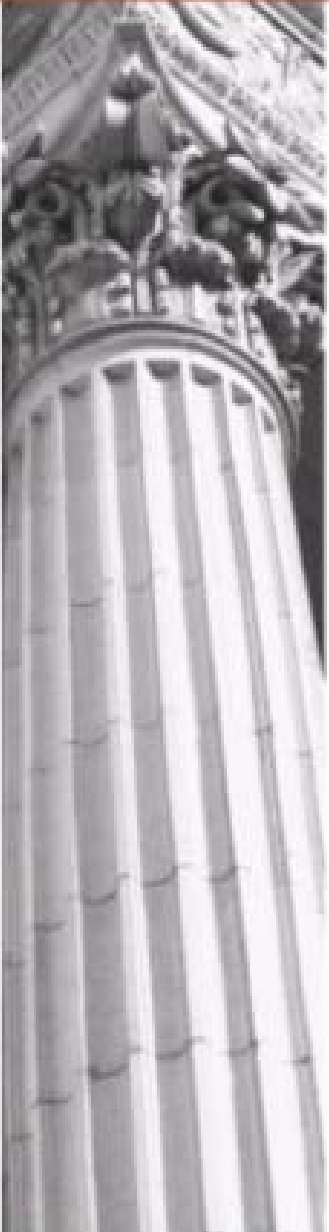


## The Local Government and School District Fiscal Accountability Act

Public Act 4 of 2011

Bettie Buss

*[www.crcmich.org](http://www.crcmich.org) / [\*\*bbuss@crcmich.org\*\*](mailto:bbuss@crcmich.org)*





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- **Statewide**
- **Nonpartisan**
- **Private not-for-profit**
- **Promotes sound policy for state and local governments through factual research**
- **Relies on charitable contributions from Michigan foundations, businesses, organizations, and individuals**



## Local control and state intervention

- Intervention in municipal financial emergencies was first authorized in PA 101 of 1988.
- School districts were included in PA 72 of 1990.
- PA 4 of 2011 grants extraordinary authority either under a consent agreement or to a state-appointed emergency manager.



## Local government revenue pressures

- Economic conditions: restructuring of the auto industry, job losses, residential and commercial foreclosures
- Declining property tax base
- Constitutional limits on property tax base and rate
- Anti-tax climate
- Federal and state deficits
- Reductions in state revenue sharing
- Reductions in state school funding



## Local government spending pressures

- Increasing health care costs for employees and retirees
- Pension costs
- Negotiated compensation costs
- Increasing demands for services
- Aging infrastructure
- Competition



## Strategies

- Use budget stabilization funds
- Freeze hiring
- Use fund balances
- Renegotiate collective bargaining agreements
- Freeze wages, impose days off without pay
- Replace D B pension plans with D C plans
- Lay off employees
- Reorganize
- Privatize
- Share services
- Eliminate services
- Consolidate



## Local control is limited by state laws

- Laws designed to ensure balanced budgets and to eliminate deficits.
- Although constitutional state revenue sharing is unrestricted, some state-source funds are restricted.
- Statutory state revenue sharing was replaced by the Economic Vitality Incentive Program in 2011.
- The Public Employment Relations Act and PA 312.
- Revision of laws to facilitate service sharing and consolidation.
- Revision of law to allow a complete state takeover.



## State strategies for ensuring fiscal responsibility in local governments

- Require balanced budgets, deficit elimination plans
- Provide incentives for accountability and transparency, consolidation of services, and reducing employee compensation costs
- Remove barriers to reducing costs
- Provide very substantive penalties for financial emergencies





## PA 72 of 1990 included a process of...

- Trigger events
- Preliminary review
- Review team review and recommendation
- Negotiated consent agreement or
- Appointment of an emergency financial manager (EFM)



## Emergency financial managers appointed under PA 72 of 1990

- City of Hamtramck 2000
- City of Highland Park 2001
- City of Flint 2002
- Inkster School District 2002
- Village of Three Oaks 2008
- City of Ecorse 2009
- City of Pontiac 2009
- Detroit School District 2009
- City of Benton Harbor 2010



## **PA 4 replaced PA 72 on March 16, 2011**

- Retains the same general process
- Enhances the role of the governor, state treasurer and superintendent of public instruction
- Provides more direction for consent agreements
- Enhances the potential role of the local chief administrative officer and other local officials
- Provides expanded powers to the emergency manager



## **“State financial authority” (SFA)**

- State treasurer for all governmental units except school districts
- State superintendent of public instruction for school districts

(The role of the local emergency financial assistance loan board is eliminated in the PA 4 process.)



## The state financial authority may conduct a preliminary review if...

- Any of the trigger events under PA 72 occur (some thresholds are lowered)
- Failure to pay benefits owed to retirees for seven days after the due date
- Breach of obligations under a deficit elimination plan
- Debt rating of BBB (the lowest investment grade) or lower
- Any other facts or circumstances that the state financial authority thinks indicate financial stress



## **Preliminary review by state financial authority**

- For a number of conditions, a written request or notification must be received. The event itself is not sufficient.
- The state financial authority must notify the local government of the review.
- Local officials are required to provide information and assistance.
- The preliminary review must be completed within 30 days.
- If the preliminary review finds probable financial stress, the governor must appoint a Review Team.



## Review Team members

- State Treasurer
- Director of Department of Technology, Management, and Budget
- Nominee of the Senate Majority Leader
- Nominee of the Speaker of the House
- Other state officials or other persons appointed by the Governor
- For school districts, all of the above plus the State Superintendent of Public Instruction
- Any of the state officials may appoint a designee to serve on the Team



## Review Team Responsibility

- Must meet with the local government.
- Must examine the books and records.
- State Department of Treasury provides staff, and the Team may use the services of other state agencies and employees.
- The Review Team may appoint an individual or firm to conduct the review.
- Must deliver its report within 60 days (one 30-day extension may be granted).
- May find no problem, severe financial stress, or financial emergency.





## Conditions indicative of severe financial stress

- All of the conditions from PA 72, with some thresholds tightened
- Failure to comply with a deficit elimination plan
- Material inappropriate interfund loans or subsidies
- A structural operating deficit
- Inappropriate use of restricted revenues
- Any other facts or circumstances indicative of financial stress or emergency in the SFA's sole discretion



## A finding of severe financial stress

- Any of the factors identified for the Review Team exist or are likely in the current or next year and may threaten the ability to provide necessary services.

OR

- The local chief administrative officer (CAO) recommends the finding.
- The Review Team may negotiate a consent agreement that provides for remedial measures necessary to resolve severe financial stress.



## Consent agreement

- Negotiated with the CAO and approved by the local governing body.
- CAO and governing body remain in place.
- May grant extraordinary powers to the CAO, CFO, governing body, or other local officials.
- Local officials are required to operate the unit in compliance with the agreement.
- May require hiring a consultant to help achieve the goals and objectives.
- After 30 days, the local unit is exempt from collective bargaining requirements, unless the state treasurer determines otherwise.



## Consent agreement content

- Continuing operations plan developed by the local government

OR

- Recovery plan developed by the state financial authority



**The continuing operations plan is the basis for local amendment of the budget and appropriations act.**

It includes:

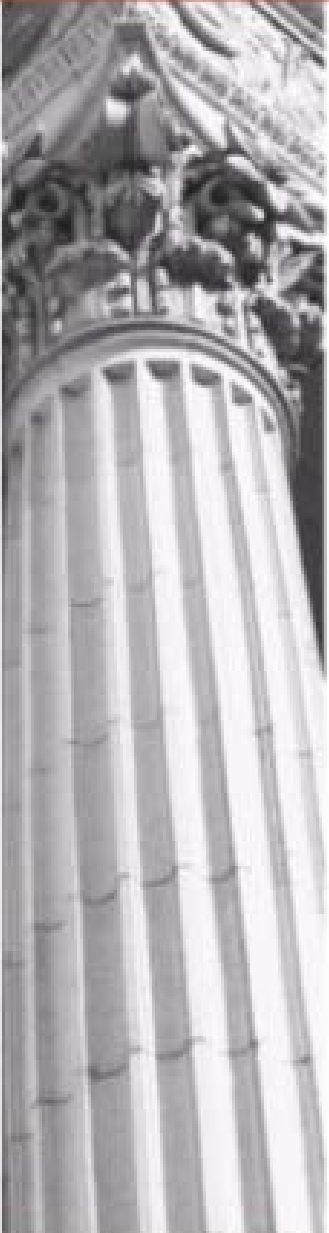
- Projected three-year budget that eliminates the deficit
- Cash flow projection for the budget period
- Operating plan
- Maintenance and capital expenditures plan
- Plan for pension and OPEB costs
- Quarterly compliance reports



## **The recovery plan supersedes the budget and appropriations ordinance.**

It may include:

- Any or all of the requirements for the continuing operations plan, plus
- Procedures for cash control and cash management
- Designated fiduciaries
- Appointment of an auditor or inspector or both



## The consent agreement

- May grant the CAO, governing body, or other local officers one or more of 31 powers of an emergency manager, including the power to reject, modify, or terminate contracts and take over an underfunded pension fund.
- May not grant the power to reject, modify, or terminate collective bargaining agreements.
- 30 days after a consent agreement is entered, the unit becomes exempt from collective bargaining requirements for the term of the agreement.



## Possible Review Team findings

- Not in financial stress or in mild financial stress
- In severe financial stress and a consent agreement has been adopted
- In severe financial stress but no consent agreement has been adopted
- A financial emergency exists





## Financial emergency definitions

- Two or more of the factors identified for the review team exist or are likely in the current year and threaten the capacity to provide necessary services.
- Failure to provide information to the review team.
- Failure to comply with a consent agreement or deficit elimination plan.
- Material breach of a consent agreement
- Severe financial stress and no consent agreement has been adopted.
- The CAO recommends the finding and the state treasurer concurs.



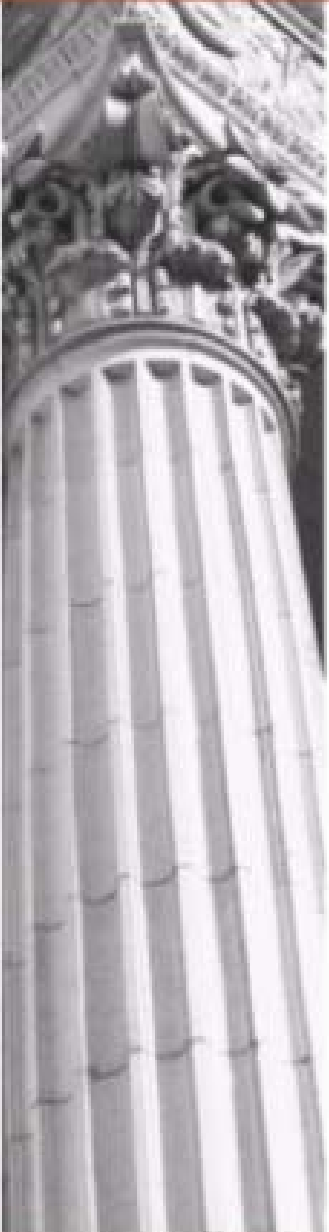
**The Governor *must* make a determination within 10 days of receiving the report.**

- Only four choices
- If an emergency is declared, the unit has 7 days to request a hearing with the governor
- If the governor affirms the emergency, the unit has 10 days to appeal to the Ingham County Circuit Court

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## **If the financial emergency is confirmed, the Governor must appoint an emergency manager.**

- An individual
- 5 years experience and expertise in business, financial, local or state budgetary matters
- Serves at the pleasure of the governor
- Paid by the local government on a contract approved by the state treasurer
- Makes quarterly reports to the state
- May be impeached as a civil officer by the state legislature



## The emergency manager

- Replaces the CAO and governing body
- Has all of the powers of an EFM under PA 72 plus additional powers
- Is responsible for operations; an EM for a school district is responsible for academics
- Orders issued to local officials, employees, contractors, and agents are binding
- Not constrained by the local charter
- The government becomes exempt from PERA



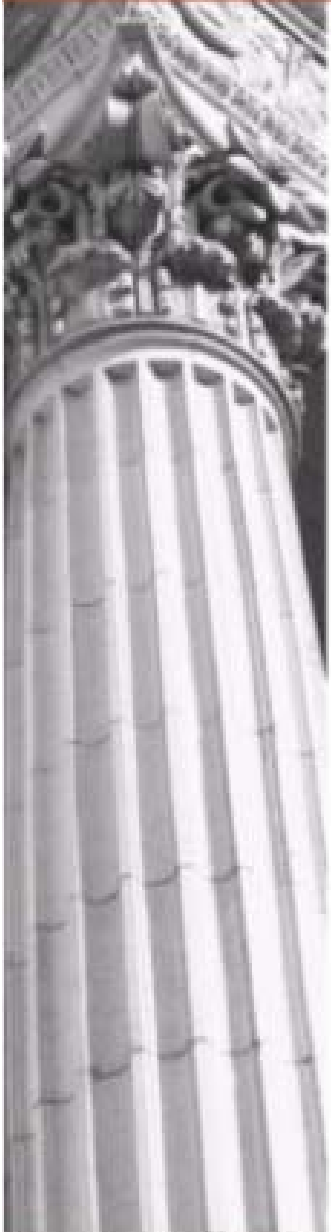
## **The EM develops the financial and operating plan to provide essential services and assure accountability**

- Conducting operations within revenues
- Payment of debt service
- Modification, rejection, termination, or renegotiation of contracts
- Required payments to the pension fund
- For a school district, an academic and educational plan
- Any other actions considered necessary by the EM



## Financial and operating plan

- Form dictated by the state treasurer
- Must be submitted to the state treasurer and, if for a school district, to the superintendent of public instruction, within 45 days
- Regularly reexamined and modified as needed
- May serve as the deficit elimination plan
- The EM must conduct a public informational meeting on the plan, but public approval is not required



## Emergency manager powers

- All of the previous powers of an EFM, plus new powers
- All financial and operating authority, including academic and educational authority in a school district
- The powers of the CAO and governing body are suspended and vested in the emergency manager; their wages and benefits are eliminated
- The unit is exempt from collective bargaining requirements



## The EM may reject, modify, or terminate one or more terms and conditions of a contract

- No restrictions on this power in the act
- May be granted to a local officer under a consent agreement
- Article I, Section 10 of the Michigan Constitution: “No bill of attainder, ex post facto law or law impairing the obligation of contracts shall be enacted”
- Article I, Section 10 of the U.S. Constitution: “No state shall...pass any Bill of Attainder, ex post facto Law, or Law impairing the Obligation of Contracts...”



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## The EM may reject, modify, or terminate collective bargaining agreements

- After meeting and conferring with the union, if, in the EM's sole discretion and judgment, a prompt and satisfactory resolution is unlikely, the EM may reject, modify, or terminate a collective bargaining agreement
- This power cannot be granted to a local officer under a consent agreement.



## Conditions for rejecting, modifying, or terminating a collective bargaining agreement

- The financial emergency makes it reasonable and necessary for the state to intercede to serve a significant and legitimate purpose.
- It is reasonable and necessary to deal with a broad, generalized economic problem.
- It is directly related to and designed to address the financial emergency for the benefit of the public as a whole.
- It is temporary and does not target specific classes of employees.



## The EM may take over a pension fund that is less than 80% funded\*

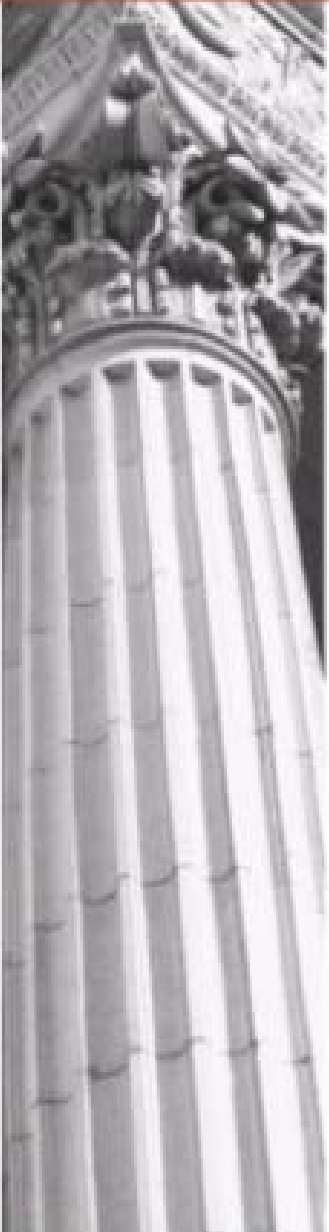
- May remove 1 or more trustees of the pension board
- State treasurer may appoint EM as sole trustee
- May assume and exercise the authority and fiduciary responsibilities of the pension board, including setting actuarial assumptions
- Must identify costs and benefits and receive the state treasurer's approval for changes
- May transfer funds from 1 pension fund to another

\*80% is net of pension bonds



## Other powers of an emergency manager

- Enter into contracts. Any contract with a cumulative value over \$50,000 is subject to competitive bidding, unless the state treasurer exempts it.
- Remove or replace appointees.
- Establish staffing levels, regardless of charter or contract requirements.
- Hire staff, including an inspector and/or auditor from an approved list.
- Consolidate or eliminate functions and departments.



## Other powers

- Schedule a millage election.
- Sell, lease, or transfer assets, with conditions.
- Apply for a state loan.
- Incur, restructure, or retire debt.
- Transfer functions and responsibilities; contract for services; provide for the joint exercise of power or consolidation of services.
- Recommend consolidation with another municipality.
- Disincorporate or dissolve a municipality.
- Request permission to file for bankruptcy.



## Reports must be filed and posted on the internet every 3 months

- Every expenditure over \$5,000.
- Every contract over \$5,000.
- Every loan over \$5,000.
- Any new position created or vacancy filled.
- Any eliminated position or position from which an employee was laid off.
- A copy of the EM's contract as approved by the state treasurer.
- Salary and benefits of the EM.
- The financial and operating plan.



## Legal protections

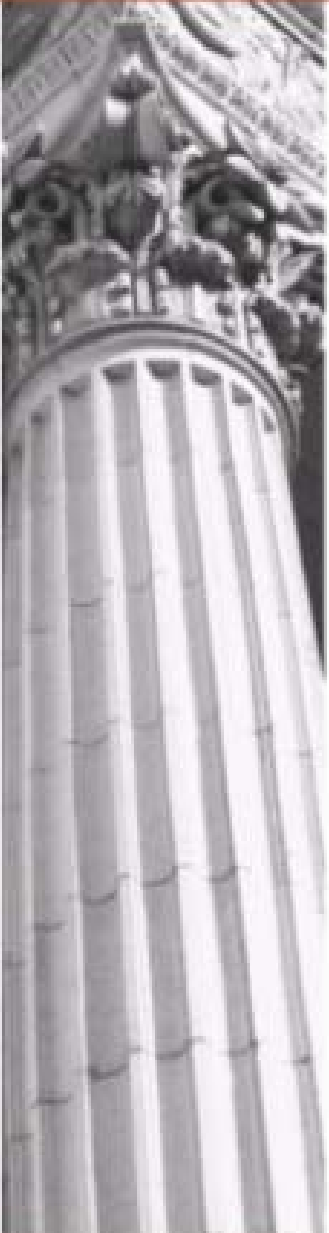
- An EM may obtain liability insurance for himself and his agents.
- Settlements and expenses not covered by insurance are to be paid by the local government if approved by the state treasurer.
- An EM is immune for liability when acting within the scope of the act.
- The state attorney general will defend any claim challenging the act, the authority of a state officer under the act, or the EM acting within the scope of the act.
- The costs of the AG are to be reimbursed by the local government.



## Failure to cooperate

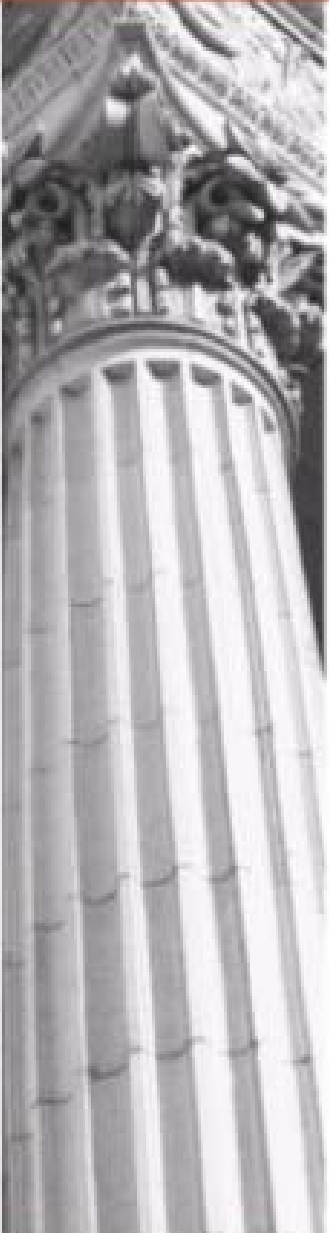
- Local officials, employees, agents, and contractors are required to cooperate with the review team and EM.
- The review team and EM may issue subpoenas and administer oaths to compel provision of information and documents.
- The review team or EM may sue in court.
- The EM may prohibit access to facilities, electronic mail, and internal information systems.
- The EM may remove appointees and fire employees.
- Failure to cooperate is gross neglect of duty, which may be reported to the state financial authority and AG. Following review and a hearing, the SFA may recommend that the governor remove an elected official.





## End of receivership

- The EM must declare the emergency resolved, the state treasurer must agree, and the superintendent of public instruction must agree for a school district.
- Before leaving, the EM must adopt a 2-year budget including all contractual and employment agreements, which cannot be amended without the approval of the state treasurer.
- The orders and ordinances adopted by the EM cannot be revised for 1 year after termination of the receivership.



## Will PA 4 be effective?

- The state's goal is to encourage local officials, unions, and contractors to agree to provide essential services within budgetary constraints.
- Local officials may be tempted to initiate the process to obtain powers under a consent agreement.
- Emergency managers will have nearly total control to impose reforms.
- Only electors can raise taxes and change charter provisions.
- Court challenges are inevitable.



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