Citizens Research Council of Michigan

CRC

Legacy Costs and Indebtedness of the City of Detroit

December 2011

Report 373

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CITIZENS RESEARCH COUNCIL OF MICHIGAN

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Overview

As City of Detroit officials struggle to reduce the city government's deficit and provide essential services, a key fiscal consideration concerns the city's liability for future payments. These costs include legacy costs for unfunded pension and other post employment benefits (OPEBs) for city government employees; the annual cost of pension obligation certificates; the principal, interest, hedging and other costs associated with bonded debt; and other contractual obligations of the city.

At June 30, 2010, all funds of the City of Detroit had $6.4 billion of outstanding bonded debt, including $5.2 billion attributable to the Water and Sewerage system, and over $600 million of other future obligations. Included in the $6.4 billion of outstanding bonded debt was $1.0 billion of general obligation debt, which equates to debt of about $1,400 per resident of the city. There will be $467.7 million of interest due on this $1.0 billion of principal; including principal and interest on general obligation debt equates to more than $2,000 per resident.

The city had $1.5 billion of outstanding pension obligation certificates and other unfunded costs associated with personnel totaling $5.6 billion: $481.5 million of unfunded actuarial accrued liability (UAAL) in the General Retirement System, $134.2 of UAAL in the Police and Fire Retirement System. Because pension obligation certificates were used to fund the pension systems, the General Retirement System was 87.1 percent funded and the Police and Fire Retirement System was 96.6 percent funded on June 30, 2010 (the General system was 65.8 percent funded and the Police and Fire system was 79.5 percent funded if the value of the pension obligation certificates was excluded).

Detroit also had $5.0 billion of UAAL for other post employment benefits, but the city continues to pay these liabilities on a pay-as-you-go basis. If the city had made the annual required contribution to fund OPEBs on an actuarial basis in fiscal 2009-10, it would have allocated $313.9 million, rather than the $149.7 million actual payment; an additional $164.2 million would have been paid from city accounts to fund future liabilities, reducing the amount available for current operations. Nonetheless, the city government's future liability for non-pension benefits promised to city retirees is about $7,000 per resident (See **Table 1**).

Table 1
City of Detroit
Legacy Costs and Other Liabilities, June 30, 2010
(Dollars in Millions)

Type of Debt, Obligation, or Liability	Amount
Non General Obligation Bonded Debt	$5,413.0
Other Post Employment Benefits UAAL	4,971.2
Pension Certificates of Participation	1,479.7
General Obligation Bonded Debt	1,010.3
General Retirement System UAAL	481.5
Police and Fire Retirement System UAAL	134.2
Other Obligations	618.5
Total	$14,108.4

Source: 2010 CAFR, Pension System Financial Reports.

Report Sources

This report includes information from the June 30, 2010 City of Detroit Comprehensive Annual Financial Report (CAFR), annual reports from the boards of trustees of the retirement systems for the fiscal year ending June 30, 2010 and financial reports for the two retirement systems, the city's 2011-12 budget, the prospectus for the distributable state aid general obligation Series 2010 limited tax bonds, and other sources. The CAFR and other reports separate city government activities into general governmental activities and business-type activities which include Water, Sewerage, Transportation, and Parking.

The amounts listed in Table 1 for bonded debt and certificates represent the principal outstanding; as noted, the amounts that will be paid on those liabilities will also include interest and could include other costs as well. Payments on the vast majority of the debt will be spread out decades into the future. Nonetheless, payments on limited tax, general obligation debt contributes to the city's cash flow problems, and further issuance of such debt will make cash flow that much more precarious. Payments for pensions and retiree benefits are also stressing the city's cash flow, even though the payments are insufficient to reduce the unfunded actuarial accrued liabilities.

Just as the kinds of future liability differ, the consequences of failing to pay these obligations when they become due also differ.

In the city's current (fiscal year 2011-12) budget, the accumulated prior years' deficit is recorded as $208.9 million. This is 13.2 percent of the total appropriations for general city agencies; it is slightly more than the net amount expected to be received from the city's property tax; and it is equal to about $300 per resident of the city. The budget defers $153.7 of the accumulated prior years' deficit to future periods, leaving a current appropriation of $55.2 million to satisfy the deficit. The operating deficit is an addition to the bonded debt, legacy costs, and other obligations described above.

Any credible deficit elimination plan must incorporate a means to resolve the city's future liabilities. Any discussion of shifting responsibility for providing services, whether to a regional transportation entity or a regional water and sewerage authority, or of controlling the growth of future costs, must also consider the obligated future costs that are associated with the services that are now provided by the City of Detroit.

Detroit's mayor, Michigan's governor, and a host of commentators have raised the possibility of state appointment of an emergency manager for the cash strapped city. This report notes the authority a financial manager would have relative to the city's various kinds of debt and liabilities.[1]

Detroit municipal income tax revenues declined from $278.3 million in 2006-07 to $212.7 million in 2009-10; current year property tax revenues for general operations declined from $183.7 million in 2006-07 to $168.0 million in 2009-10. With local tax revenue reductions exacerbated by reductions in state revenue sharing payments, the city's strategy of financing current operations with future revenues is not sustainable. Without major structural changes, limited tax debt, pensions, and other post employment benefits will continue to absorb increasing amounts of the general fund, leaving less and less for essential public services.

Pension Obligations and Other Post Employment Benefit Obligations, Defined

Pension plans are established to hold the assets that will be needed to pay the pensions that have been promised to qualified employees when those pensions

[1] For a more complete description of the Local Government and School District Fiscal Accountability Act, PA 4 of 2011, please see Citizens Research Council Report 368, April, 2011 www.crcmich.org/PUBLICAT/2010s/2011/rpt368.html.

[2] June 30, 2010 City of Detroit Comprehensive Annual Financial Report, page 29.

are due. If the city receives labor services from an employee and a pension is part of that employee's compensation, the city must deposit sufficient funds to pay that future obligation in a trust fund.

Pension obligations derive from contractual agreements between the city government and city employee unions. The Michigan Constitution (Article IX, Section 24) provides that "The accrued financial benefits of each pension plan and retirement system of the state and its political subdivisions shall be a contractual obligation thereof which shall not be diminished or impaired thereby." This does not mean that the state insures or guarantees payment from local governments, but that individuals who have earned a pension from a public employer have the right to sue to have the contractual obligation met by that employer.

> "The accrued financial benefits of each pension plan and retirement system of the state and its political subdivisions shall be a contractual obligation thereof which shall not be diminished or impaired thereby." Michigan Constitution (Article IX, Section 24)

The Michigan Constitution also provides that "Financial benefits arising on account of service rendered in each fiscal year shall be funded during that year and such funding shall not be used for financing unfunded accrued liabilities." "Normal costs" are the costs associated with the service rendered in that fiscal year. Normal costs can be reduced if the government negotiates lower pension benefits going forward, switches to a defined contribution plan, or closes the defined benefit system. If the city were to close the defined benefit plan, the obligations to past employees would remain and the city would be required to continue funding those liabilities. Closing the defined benefit plan could result in annual city contributions increasing in the near term.

"Unfunded actuarial accrued liabilities" (UAAL) is the difference between the value of assets in the pension fund and the present value of all of the future pension payments that have been earned by employees. Employers (and employees in systems where they participate in funding) are supposed to pay all of the "normal cost" and pay enough of the unfunded actuarial accrued liabilities to retire that obligation over not more than 30 years (some systems have adopted shorter amortization periods).

Unfunded accrued actuarial liabilities may exist for a number of reasons: not enough was paid into the fund annually; the assets in the fund lost value due to stock market losses or other losses; the assumptions about future earnings or longevity or inflation or other factors were incorrect; or other reasons. Most defined benefit retirement systems (those are systems that promise a defined pension payment based on years of service and other factors) have some unfunded actuarial accrued liability, and experts consider 80 percent funding to be acceptable for public systems that are expected to exist in perpetuity. Failure to make required annual payments into the pension fund may result in higher required contributions in future years to make up the difference, but if the value of system assets such as stocks, bonds, and real estate increase above the assumed rate, the future payments will decrease or may even be unnecessary.

If the pension fund is unable to make required payments to retirees, retirees may sue to force payment. This could trigger state intervention under PA 4 of 2011. In some instances where retirees have sued, a judge has ordered the imposition of a judgment levy to fund pensions. Imposition of a judgment levy without the prior approval of the local governing body is one of the events that can trigger a preliminary review under PA 4.

Some governments, including Detroit, have opted to fund their pension systems with the proceeds from the sale of bonds or certificates of indebtedness. This strategy is a bit of a gamble that could work to the government's advantage if the arbitrage that is the basis of the concept works as expected (arbitrage involves borrowing at a lower rate, usually because it is tax free, and investing the proceeds at a higher rate of return). However, if the costs of borrowing exceed the return on invested proceeds, this strategy can both increase costs and increase the consequences associated with nonpayment. For example, in 2005, Detroit issued $640 million in pension funding certificates with interest rates ranging between 4.00 and 4.95 percent; more certificates were issued in 2006. Proceeds were invested in the city's pension funds where the assumed actuarial rate of return was just under 8 percent. If the pension plan assets grew at the assumed rate, the invested bond proceeds would have investment earnings sufficient to cover the debt service, with earnings left over to support the plan. The risk associated with the arbitrage strategy is that the debt service payments are fixed, while the earnings on the invested proceeds depend on the earnings of the overall pension plan, which fluctuate with market conditions. It is possible that the pension returns could exceed the actuarial assumption, in which case the bonds would prove to be a good investment, or the investment returns could fall short of the actuarially assumed rate of return. In fact, the stock market has been extremely volatile in the years since the city sold pension certificates of participation: the S&P 500 stock market returns were +11.6 percent in 2007; +1.9 percent in 2008; -32.3 percent in 2009; and +12.4 percent in 2010. Both of Detroit's retirement systems suffered negative composite returns in 2008 and 2009 (See **Table 2**).

In the case of *Studier v. Michigan Public School Employees' Retirement Board*, 698 N.W.2d 350 (MI Supreme Court 2005), the state Supreme Court found that "health care benefits are not 'accrued financial benefits' and, thus, are not protected by Const 1963, art 9, S 24."

As will be described later in this report, other complexities can arise as well. "Other post employment benefits" (OPEBs) may include health, dental, vision, and life insurance promised to qualified employees when they retire. Traditionally, OPEBs were paid on a pay-as-you-go basis; no reserves were built up, as for pensions. In the case of *Studier v. Michigan Public School Employees' Retirement Board*, 698 N.W.2d 350 (MI Supreme Court 2005), the state Supreme Court found that "health care benefits are not 'accrued financial benefits' and, thus, are not protected by Const 1963, art 9, S 24."

In July 2004, the Governmental Accounting Standards Board (GASB) issued Statement No. 43 and Statement No. 45 which established accounting and financial reporting standards for public employers that have defined benefit OPEBs. The standards were intended to ensure that governments account for the annual cost of OPEB and for the unfunded actuarial accrued liabilities for those financial obligations. In essence, GASB requires that governments account for OPEBs just as they account for pensions. There is no penalty for continuing to finance these obligations on a pay-as-you-go basis, but the full amount of the un-

Table 2
Investment Returns

		Total Fund Composite Return	
	S&P 500 Stock Market Returns	General System	Police and Fire System
2010	12.4%	8.0%	16.9%
2009	-32.3	-18.8	-14.8
2008	1.9	-4.3	-6.3
2007	11.6	18.9	17.4
2006	8.2	11.3	11.5
2005	7.6	8.3	8.2

Source: S&P 500 Stock Market Returns from www.economy.com/freelunch, CRC calculations of the annual growth for July to June time periods; June 30, 2010 Financial Report: Police and Fire Retirement System of the City of Detroit; June 30, 2010 Financial Report: Pension Plan of the General Retirement System of the City of Detroit.

funded future liability must appear in the annual financial reports of the government.

Since adoption of the GASB standards in 2004, prefunding of OPEB obligations has taken on greater importance. Some governments (including Oakland County) have borrowed to fund OPEB obligations with the intent of reducing annual contributions. The risks associated with this debt are the same as those for pension funding bonds with the added complexity that, while pensions are constitutionally protected, OPEBs are not. Sale of OPEB funding bonds or certificates locks the local government into a liability which it would not otherwise have and which it could potentially avoid or reduce (to the detriment of retirees).

Indebtedness

Governments incur other future liabilities resulting from contractual and legal obligations. The City Detroit has various kinds of debt and other future obligations, and the penalties and consequences associated with the different kinds of liabilities vary from inconsequential to very substantial. On June 30, 2010, the city had $5.7 billion of bonded debt outstanding, of which $1.0 billion was general obligation bonds backed by the full faith and credit of the city. In addition, the city's governmental activities had debt of $2.0 billion for

- pension obligation certificates ($1.2 billion),
- notes payable ($89.5 million),
- loans payable ($37.9 million),
- other post employment benefits ($360.6 million),
- and other obligations ($314.4 million).[2]

Detroit general government debt totaling over $3.0 billion equates to a debt of $4,230 per capita for the 713,777 residents reported in the 2010 census. There was, in addition, other debt associated with enterprise (business type) activities of the city, primarily water and sewerage.

> Some of Detroit's limited tax debt has been secured by specific general fund revenues such as distributable state aid. This is essentially money borrowed for operations that has an annual cost that is paid out of the general fund. Debt service on limited tax debt would otherwise be available for services including police and fire protection, public health, public lighting, parks and recreation, and other services to citizens.

Bonded Debt Defined

"Bonded debt" occurs when the city sells bonds to investors: the city receives the payment for the bonds and promises to repay the principal amount borrowed plus interest over a period of years. The source of the repayment determines whether the bonds are "general obligation" (also referred to as "full faith and credit") or "revenue" bonds.

States place limits on the amount of debt a local government may have outstanding at any one time in order to ensure that the local government has the resources necessary to meet obligations when due. The Home Rule Cities Act (PA 279 of 1909) generally limits the amount of some kinds of municipal debt outstanding to ten percent of the assessed value of real and personal property in the city. As of June 30, 2010, Detroit's debt limit was $1.2 billion and the city had $919.6 million of debt applicable to the limit, leaving a legal debt margin of $299.1 million (about 25 percent). Most of the city's $6.4 billion of bonded debt is not subject to the statutory debt limit (including $5.2 billion in revenue bonds guaranteed by the water and sewerage system).

General obligation bonds are backed by the full taxing and borrowing power of the city, not by any collateral. The city's below investment grade bond rating has increased the cost of interest that must be paid on general obligation bonds. General obligation bonds are either "limited tax" bonds or "unlimited tax" bonds.

Limited tax bonds do not require voter approval and are repaid from the general operating revenues of the city. Some of Detroit's limited tax debt has been secured by specific general fund revenues such as distributable state aid. This is essentially money borrowed for operations (such as deficit reduction) that has an annual cost that is paid out of the general fund. Debt service on limited tax debt would otherwise be available for services including police and fire protection, public health, public lighting, parks and recreation, and other services to citizens.

Failure to pay debt service on bonds is termed "default" and may result in restructuring the payments and/or in state intervention under the Local Government and School District Fiscal Accountability Act (PA 4 of 2011).

Unlimited tax bonds must be approved by the voters and are repaid from a special property tax levy (the debt service levy). Unlimited tax bonds do not put pressure on the city's operating budget, but do increase the burden on the city's tax payers. The debt service levy does not count toward the statutory limit of 20 mills which may be levied for general operations. The debt service millage rate is set at a level that is sufficient to repay the principal and interest due on the outstanding bonds in that year.

Revenue bonds do not require voter approval and are secured by specified revenues from a particular source, such as customer payments to the water system. The holders of revenue bonds have no claims on the general tax or other revenues of the government; they have a claim only on the particular revenue that was pledged for the bonds. Revenue bonds that are guaranteed by sources of revenue that are outside the city's general fund do not affect the city's ability to provide basic services. In the case of Detroit, for example, water and sewer bonded debt does not affect the general city's operating budget at all.

As noted, there are different consequences for failing to pay different kinds of obligations. Failure to pay debt service on bonds is termed "default" and may result in restructuring the payments and/or in state intervention under the Local Government and School District Fiscal Accountability Act (PA 4 of 2011). A default situation would seriously affect a city's credit rating, access to future credit, and the cost of future borrowings.

Future Costs Associated with Employees

In 2010, the City of Detroit government was the second largest employer in Detroit, and the financial circumstances that affect the 12,300 city employees and 20,000 retirees (approximate numbers as of June 30, 2010) have a significant effect on the economy of the city. At the same time, the costs associated with current and retired employees are a part of the city's ongoing financial challenge. **Table 3** shows the current costs associated with active and retired employees from the city's FY2012 budget.

In the current fiscal year, contributions to the city's General Retirement System and Police and Fire Retirement System will cost general city agencies $147.2 million, or 10.3 percent of the general city operating budget. Fringe benefits for retirees are expected to cost general city agencies $124.7 million, or 8.7 percent of the general city operating budget. In comparison, total appropriations for the Department of Public Works are $114.4 million (8.0 percent of the general city operating budget); the Department of Health and Wellness budget is $77.4 million (5.4 percent); the Public Lighting Department budget is $53.9 million (3.8 percent). The total budgeted prior years' deficit is $208.9 million.

City of Detroit Retirement Systems

The Michigan Constitution makes pension benefits that have been earned by state and local government employees a contractual obligation of the public employer, although benefits that have not yet been earned may be renegotiated. In addition to the constitutional guarantee, the City of Detroit is obligated under the city charter and union contracts to pay pensions earned by city government employees.

Table 3
City of Detroit Appropriations for Personal Services, 2011-12
(Dollars in Millions)

	General City Agencies	Enterprise Agencies	Total
Salaries and Wages	$437.8	$169.3	$607.1
Payments to Pensions Funds*	$147.2	$44.5	$191.8
Fringe Benefits for Retirees			
Hospitalization	$117.4	$30.7	$148.1
Other (Dental and Eye Care)	7.3	1.9	9.2
Total OPEBs	$124.7	$32.6	$157.3
Fringe Benefits for Active Employees			
Hospitalization	$75.7	$34.8	$110.5
Other	48.2	23.1	71.3
Total Active Fringes	$123.9	$57.9	$181.8
Total Fringe Benefits	$395.8	$135.0	$530.8
Total Personal Services	$833.6	$304.3	$1,137.9
Total Operating Budget**	$1,426.8	$1,070.5	$2,497.3

*Including pension obligation certificates

**Excludes bonded capital and debt service

Source: City of Detroit Budget, 2011-12

These costs include retirement, disability and survivor benefits paid from two pension funds, a General Retirement System for civilian employees and a Police and Fire Retirement System for uniformed employees. These are very large funds, with $2.2 billion of net assets in the General Retirement System and $3.0 billion of net assets in the Police and Fire Retirement System.[3] Each fund includes a defined benefit plan funded by the city and a defined contribution (annuity) plan funded by employees. And in spite of the sale of $1.6 billion of pension funding certificates in 2005 and 2006, each fund has an unfunded actuarial accrued liability (the most recent reports from the pension systems indicated combined UAAL of $615.7 million). In Fiscal Year 2011-12 (FY2012), the city appropriated $191.8 million for payments to the pension funds.

The General Retirement System

On June 30, 2010, there were 8,072 active members and 11,539 retirees and beneficiaries in the general system. Active employees had average pay of $41,420 and 15.3 years of service (both average age and length of service are increasing due to layoffs based on seniority, which ends employment for younger workers with fewer years of service). Employees earn pension benefits based on years of service and average final compensation; annuity distributions are based on the employee's contributions.

Employee contributions to the annuity savings fund are voluntary and may be 0 percent, 3 percent, 5 percent, or 7 percent of gross pay. After 25 years of service, an active employee may chose to withdraw his or her accumulated contributions plus any investment earnings. On retirement, an employee may elect to purchase an annuity with some or all of the money in his or her annuity savings account, resulting in a larger monthly retirement benefit. Any remainder in the account is paid to the employee.

Retirees and beneficiaries of the General Retirement System received an average annual payment of $17,587.

The city's costs for employee pensions are calculated and budgeted on a percent of payroll basis. One consequence of this approach is that reductions in the number of active employees can result in increasing percentages because the cost of the unfunded actuarial accrued liability (UAAL) is spread

[3] June 30, 2010 City of Detroit Comprehensive Annual Financial Report, page 174.

Table 4
General Retirement System,
Required Employer Contribution as a Percent of Payroll
Valuation of June 30, 2010*

	Normal Cost	UAAL	Total	Percentage Point Increase from Prior Year
General City	11.22%	4.04%	15.26%	1.89%
DOT	10.04	10.22	20.26	4.92
Water/Sewerage	11.00	14.82	25.82	6.19
Library	10.88	11.27	22.15	4.92
Total	10.97%	8.14%	19.11%	3.73%

*The valuation of June 30, 2010 determines contributions on a percent of payroll basis for FY 2012.

Source: Annual Report of the Board of Trustees for the Year Ending June 30, 2010, General Retirement System, page 14.

over a smaller number of employees. Voluntary employee contributions are also on a percent of payroll basis. According to the 2010 Annual Report of the Board of Trustees of the General Retirement System, required employer contribution rates for each of the component units of the General Retirement System (General City, Department of Transportation, Water and Sewerage, and the Detroit Public Library) will increase in FY2012. For example, the percent of payroll required for general city employees increased from 13.37 in FY2009 to 15.26 in FY2010; the percent of payroll required to fund pensions for Transportation employees increased from 15.34 in FY2009 to 20.26 in FY2010 (See **Table 4**).

Current assets, future needs, and various assumptions are used to determine how much the city should contribute to the pension system each year. In FY2010, the city government contribution to the General Retirement System was $37.3 million and employee contributions to the annuity fund were $19.0 million ($56.3 million in total); the system paid $211.3 million in benefits plus $104.7 million in lump sum defined contribution plan benefits ($316.0 million in total). The most recent CAFR reported total net assets in the General Retirement System of $2,246.5 million. The unfunded actuarial accrued liabilities in the General system were $481.5 million at June 30, 2010 (up from $276.7 million at June 30, 2009), and were 144.0 percent of covered payroll. The system was 87.1 percent funded, inclusive of the proceeds of pension obligation certificates.[4] This is well in excess of the 80 percent funding threshold for public defined benefit plans, but the debt arising from the certificates, normal costs, and UAAL remains a substantial burden for the city government.

In the FY2012 budget, the city appropriated $51.9 million for payments to the General Retirement System for civilians in general city agencies and $44.5 million for payments to the General Retirement System for employees in enterprise agencies, a total of $96.4 million for civilian pension contributions.

> In the FY2012 budget, the city appropriated $51.9 million for payments to the General Retirement System for civilians in general city agencies and $44.5 million for payments to the General Retirement System for employees in enterprise agencies, a total of $96.4 million for civilian pension contributions. The city also appropriated $95.3 million for payments to the Police and Fire Retirement System for a total FY2012 cost of $191.7 million.

The Police and Fire Retirement System

In FY2010, there were 8,356 retired members of the Detroit Police and Fire Retirement System (DPFRS) and they received an average annual allowance of $29,163. There were 3,992 active members of the system (2,927 Police and 1,065 Fire); the number of active members has been declining (there were 5,585 active members in 2001). In 2010, the average Police member was 41.8 years old, with 15.1 years of service and annual pay of $56,217. The average Fire member was 43.7 years old with 17.7 years of service and annual pay of $60,359.

Uniformed employees in ranks of sergeant and above are eligible to retire after 25 years of service; members of the Detroit Police Officers Association and their Fire equivalents are eligible to retire after 20 years of service regardless of age. Employees earn pension benefits based on their years of service and average final compensation; benefits differ for "pre 1969 members" and "1969 plan members." For members in the "1969 plan," the annual pension amount is 2.5 percent of the average final compensation times the first 25 years of service plus 2.1 percent of average final compensation times each of the next ten years of service. Members may elect to withdraw their accumulated contribution amount in a lump sum, and if they do, the defined benefit is reduced by the actuarial equivalent of the amount withdrawn. In FY2010, payments of benefits to retirees and beneficiaries in the DPFRS totaled $251.7 million and $27.3 million was paid in lump sum defined contribution plan benefits.

[4] Annual Report of the Board of Trustees for the Year Ending June 30, 2010, General Retirement System

The DPFRS system was overfunded in 2006 through 2008 as a result of the city's sale of pension obligation certificates in 2005 and 2006. However, the value of assets in the system declined from nearly $5.0 billion at June 30, 2008 to less than $3.5 billion at June 30, 2010 due to losses in the stock market and real estate market. The most recent CAFR reported total net assets in the Police and Fire Retirement System of $3,017.9 million. In FY2009, the unfunded actuarial accrued liability in the Police and Fire Retirement System was $276.1 million. In FY2010, the UAAL was reported to be $134.2 million (58.7 percent of covered payroll) and the system was 96.6 percent funded, including the proceeds from the pension funding bonds. However, the funding value of assets in the system exceeded the market value by $835 million, and unless the market recovered quickly, another large increase in the required employer contribution was predicted.[5]

In April, 2011, arbitrator Thomas W. Brookover found that Police and Fire pension obligations threatened Detroit's fiscal viability and ruled that the city could reduce pensions earned in the future by the members of the Police Sergeants and Lieutenants Association. In August, 2011, the city and the Detroit Police Officers Association reached their first voluntary, consensual settlement achieved through collective bargaining in 32 years (outside of the PA 312 of 1969 binding arbitration system). The DPOA ratified a one-year agreement that not only froze wages, but also reduced pensions for current officers by reducing the multiplier for benefits earned after September 1, 2011 from 2.5 to 2.1 percent of average final compensation and eliminating cost of living increases on pensions earned after that date. Additionally, officers hired after July 1, 2012 would join a defined contribution plan, to which the city would contribute an amount equal to ten percent of the employee's salary. Over the long term, these changes should reduce employer contributions to the Police and Fire Retirement System.

The DPOA ratified a one-year agreement that not only froze wages, but also reduced pensions for current officers by reducing the multiplier for benefits earned after September 1, 2011 from 2.5 to 2.1 percent of average final compensation and eliminating cost of living increases on pensions earned after that date. Additionally, officers hired after July 1, 2012 would join a defined contribution plan, to which the city would contribute an amount equal to ten percent of the employee's salary.

The employer contribution for FY2010 was $57.8 million, less a negotiated $25.0 million overfunding credit, for a city payment of $32.8 million. The employee contribution to the annuity plan was $10.8 million. The employer contribution rate for FY2012 was calculated to be 27.81 percent of payroll, or 28.90 percent if paid at year end. In the FY2012 budget, the city appropriated $95.3 million for payments to the Police and Fire Retirement System, a much larger amount than the $51.9 million appropriated for payments to the General Retirement System for civilians in general city agencies and approximately equal to the $96.4 million appropriated for all payments, including water and sewerage payments, to the General Retirement System.

Pension Obligation Certificates

In 2005 and 2006, the city sold $1.6 billion of variable rate pension certificates of participation (COPs) to fully fund both retirement systems, transforming pension funding obligations into contractual obligations to pay the principal and interest on the certificates (and possibly increasing the severity of consequences for nonpayment).

The issuance of pension funding bonds or certificates can produce savings if the interest rate paid

[5] Annual Report of the Board of Trustees for the Year Ending June 30, 2010, Detroit Police and Fire Retirement System.

[6] GFOA Advisory, Evaluating the Use of Pension Obligation Bonds (1997 and 2005), March 2005.

on the bonds is less than the rate of return earned on proceeds placed in the pension fund.[6] The city entered into eight swap agreements to establish a fixed rate on the pension certificates, and these swap agreements included a number of provisions to protect the rights of the participants. Specifically, the agreements provided that a "termination event" would occur if the credit rating on the COPs was withdrawn or downgraded to below a certain level (Baa3) and if the bond insurers' credit rating fell below a certain level (A3). In January, 2009 the city was informed that events had occurred that would constitute a termination event and in June the parties entered into a collateral agreement that increased the amount of payments, required the city to deposit daily casino wagering tax revenues with a trustee to ensure payments due under the swap agreements, and established new conditions.

The debt for the certificates of participation is in addition to the $615.7 million UAAL for the two pension systems, and is in addition to the bonded debt discussed in a later section of this report. However, the appropriation for actuarial pensions in the FY2012 city budget includes the payment on the pension obligation certificates. (See **Table 5**.)

As of June 30, 2010, the date of the most recent CAFR, the principal outstanding on the certificates was $1.5 billion, but the total amount of future payments (principal and interest) associated with those bonds was $2.9 billion and the debt by government activity is shown in **Table 6**.

Table 5
Service Payments on 2005 and 2006 Certificates of Participation, (Dollars in Millions)

Year Ending June 30	Total Payment
2011	$96.1
2012	101.6
2013	107.1
2014	112.6
2015	114.8
2016	117.0
2017	119.2
2018	121.5
2019	119.8
2020	119.7
2021	119.7
2022	119.7
2023	119.7
2024	119.7
2025	119.7
2026	119.7
2027	119.6
2028	119.6
2029	119.5
2030	119.4
2031	119.3
2032	119.3
2033	119.2
2034	119.1
2035	119.0

Source: Prospectus for Distributable State Aid General Obligation Bonds, Series 2010, page A-51.

Table 6
Pension Obligation Certificates Outstanding Debt June 30, 2010 (Dollars in Millions)

	Principal	Interest	Other*	Total
General Govt. Activities	$1,202.9	$482.8	$689.2	$2,375.0
Transportation Fund	105.9	42.5	60.7	209.1
Sewerage Fund	90.8	36.4	52.0	179.2
Water Fund	80.1	32.2	45.9	158.2
Total	$1,479.7	$594.0	$847.9	$2,921.6

*Hedging, derivatives, etc.

Source June 30, 2010 City of Detroit Comprehensive Annual Financial Report, page 108-109.

Table 7
Detroit Retirement Systems, June 30, 2010
(Dollars in Millions)

	General Retirement System	Police and Fire Retirement System
Total Actuarial Accrued Liability	$3,719.6	$3,987.5
Total Value of Assets	$3,238.1	$3,853.3
Unfunded Actuarial Accrued Liability	$481.5	$134.2
Total Assets / Total Liability	87.1%	96.6%
Pension Obligation Certificate (POC)	$789.7	$680.9
Total Value of Assets – POC	$2,448.4	$3,172.4
Net Assets / Total Liability	65.8%	79.5%

Source: 2010 Annual Reports of the Board of Trustees, CRC calculations

In spite of asset losses since the sale of COPs, the city's pension funds appear to be adequately funded when the value of the pension obligation certificates is included in fund balances. There are, however, questions about the value of some pension assets. Independent auditors' reports by Plante & Moran dated June 30, 2010 noted that they were unable to obtain sufficient audit evidence supporting $103.0 million of alternative investments in the Police and Fire System and $113.0 million in the General System, and that financial statements include investments valued at $835.0 million in the Police and Fire System and $710.0 million in the General System "whose fair values have been estimated by management in the absence of readily determinable fair values."

It should be noted, however, that PA 4 of 2011 allows a state-appointed emergency manager to remove one or more of the trustees of a local pension board, and allows the state treasurer to appoint the emergency manager as the sole trustee of a local pension board, if the pension fund is not actuarially funded at 80 percent or more, excluding the net value of pension bonds or evidence of indebtedness.[7] (See **Table 7**.)

Without the value of pension obligation certificates, neither of Detroit's two pension system meets the 80 percent funding threshold established in PA 4; both would be subject to takeover by an emergency manager.

[7] PA 4 of 2011, Sec. 19 (1)(m).

Other Post Employment Benefits

In addition to pensions, the city has negotiated with employee unions the payment of other post employment benefits (OPEBs) including health insurance. These benefits for retirees have been funded on a "pay as you go" basis, which means that the cost of benefits billed in each year were paid that year, but no amount was set aside to pay for future benefits that had already been earned. The increasing number of retirees and the increasing cost of health care result in increasingly expensive OPEB costs.

The city's Health and Life Insurance Benefit Plan provides hospitalization, dental care, vision care, and life insurance to eligible retirees. (In addition to this plan, the city maintains a supplemental death benefit plan which had an unfunded actuarial accrued liability of $5.6 million.) According to the 2010 CAFR, the city pays for full health care coverage, except for master medical coverage, for general city employees who retired before January 1, 1984. The city pays up to 90 percent of coverage for general city retirees who retired after January 1, 1984 and for Police and Fire retirees. The city also pays for health care for the retiree's spouse as long as the spouse continues to receive a city pension (the city does not pay for health care coverage for a new non-city retiree spouse). The city pays for dental and vision coverage for the retiree and spouse in both systems. The city does not pay for health care coverage for employees who take early retirement. Complementary health care coverage is provided to retirees who are Medicare eligible.

As noted previously, GASB now requires that the future liability for promised post employment benefits be included in financial reports, just as the UAAL for pensions is reported. As of the June 30, 2009 actuarial valuation, the unfunded actuarial accrued liability for OPEBs for all Detroit city employees was approximately $5 billion ($4,971.2 million), none of which was funded. The covered payroll of the city was $591.2 million, and the ratio of the UAAL to payroll was 841 percent.[8] The OPEB UAAL debt per resident of Detroit was approximately $7,000, though amounts for the water and sewerage system will be paid by customers of that system. (The Detroit Water and Sewerage Department provides water and sewerage services for Detroit and for approximately three million people in 126 other communities in eight counties.) There is no expectation that funding for such a large total liability would be made available in the near term, but rather that prudent financial management would seek to fully fund the liability over a period of 30 years or less.

Retirees are generally required to pay 10 or 20 percent of health insurance premiums. In FY2010, the amount paid by all funds of the city for OPEBs was $149.7 million, which was the "pay-as-you-go" amount. (See **Table 8**.)

[8] June 30, 2010 City of Detroit Comprehensive Annual Financial Report, page 121.

Table 8
Health and Life Insurance Benefit Plan, FY 2009-10
(Dollars in Millions)

Benefit	City Payment	Retiree Payment	Total
Hospitalization	$140.4	$23.7	$164.1
Dental	7.8	1.3	9.1
Vision	1.3	-	1.3
Life Insurance	0.2	-	0.3
Total	$149.7	$25.0	$174.7

Source: June 30, 2010 City of Detroit Comprehensive Annual Financial Report, page 119.

Table 9
Other Post Employment Benefits, June 30, 2010
(Dollars in Millions)

	Annual Required Contribution	City Payment
Governmental activities	$246.8	$122.6
Transportation Fund	26.1	10.4
Sewage Disposal Fund	20.8	8.3
Water Fund	19.3	8.0
Automobile Parking Fund	0.7	0.2
Non-major Proprietary Fund	0.2	0.1
Total	$313.9	$149.7

Source: June 30, 2010 City of Detroit Comprehensive Annual Financial Report, page 120.

The city's FY2010 payment was less than half of the amount needed to fund OPEBs on an actuarial basis. For FY2010, a city contribution of $313.9 million (the "annual required contribution" or ARC) was required both to cover the normal cost of OPEBs and to amortize the unfunded actuarial accrued liability over not more than 30 years. This annual required contribution by fund, and the amount actually paid by fund, is shown in **Table 9**.

Since the ARC was not fully funded in FY2010, the amount due to meet this liability increased from June 30, 2009 to June 30, 2010. The change in this liability by fund is shown in **Table 10**.

In the current year budget, the city has appropriated $157.3 million to pay for retiree hospitalization, dental benefits, and eye care. That is 6.3 percent of the city's total operating budget (including enterprise agencies), but is insufficient to actuarially fund OPEBs.

Oakland County, Michigan has approached the issue of other post employment benefits in a different fash-

Table 10
Changes in Long-Term Obligation for Accrued Other Post Employment Benefits
(Dollars in Millions)

	June 30, 2009	June 30, 2010	Increase 2009 to 2010
Governmental Activities	$236.3	$360.6	$124.3
Transportation Fund	28.9	44.7	15.8
Sewage Disposal Fund	17.9	30.5	12.6
Water Fund	16.6	27.9	11.3
Automobile Parking Fund	0.4	0.9	0.5
Other Proprietary Funds	0.1	0.2	0.1
Total	$300.2	$464.8	$164.6

Source: June 30, 2010 City of Detroit Comprehensive Annual Financial Report, pages 92-96.

ion. The county began actuarially funding OPEBs in 1987 and in 2007 the county issued certificates of participation to fully fund its existing health care obligation for current and future retirees.

While state and local government pensions that have been earned are protected in the state Constitution, future pensions and other post employment benefits do not have the same protection and can be renegotiated to reduce future costs to the city. Annual increases in the cost of health care, increased longevity, declining tax base, reduced state aid, and other factors combine to make it increasingly unlikely that the city government can afford to maintain the level of current and future benefits city workers have negotiated. If the city's administration and unions are unable to renegotiate future benefits to reduce costs, PA 4 of 2011 provides for a different approach whereby an emergency manager is granted power to reject, modify or terminate contracts and to reject, modify, or terminate collective bargaining agreements under specified conditions.

In spite of the conclusion reached by the Michigan Supreme Court in the *Studier* case, it is highly probable that retirees would litigate the issue if health care coverage for retirees were reduced or eliminated.

Bonded Debt Service

All large cities use debt to fund capital improvements, major maintenance, and for other purposes, under limits established in state laws. In 2009, according to the U.S. Census Bureau, there was a total $1.6 trillion of U.S. local government debt outstanding (the total amount of state and local government debt outstanding was $2.6 trillion).

Bond Ratings

Credit rating agencies rate city governments and other public and private entities on a number of criteria designed to measure their ability to repay bonded debt, and assign alphanumeric ratings that indicate the risk associated with the outstanding debt. The "big three" rating agencies are Standard and Poor's, Moody's, and Fitch Ratings, each of which has its own system for rating borrowers (See **Table 11**).

Lower bond ratings indicate higher risk and justify investors' demands for higher interest rates on those bonds.

Table 11
Long Term Bond Ratings

Definition	Standard & Poor's	Moody's	Fitch
Maximum safety	AAA	Aaa	AAA
High quality	AA+,AA,AA-	Aa1,Aa2,Aa3	AA+,AA,AA-
Upper medium grade	A+,A,A-	A1,A2,A3	A+,A,A-
Lower medium grade	BBB+,BBB,BBB-	Baa1,Baa2,Baa3	BBB+,BBB,BBB-
Non investment grade	BB+	Ba1	BB+
Speculative	BB,BB-	Ba2,Ba3	BB,BB-
Highly speculative	B+,B,B-	B1,B2,B3	B+,B,B-

Detroit has the lowest bond rating among the largest U.S. cities. The city's general obligations are rated "non investment grade." (See **Table 12**.)

Table 12
Bond Ratings for Select City Governments, 2010

City	Standard & Poor's	Moody's	Fitch
Phoenix, AZ	AAA	Aa1	(NA)
San Antonio, TX	AAA	Aa1	AAA
Columbus, OH	AAA	Aaa	AAA
Minneapolis, MN	AAA	Aa1	AAA
Dallas, TX	AA+	Aa1	(NA)
New York, NY	AA	Aa3	AA
Houston, TX	AA	Aa3	AA
Indianapolis, IN	AA	Aa1	(NA)
Milwaukee, WI	AA	Aa2	AA+
Los Angeles, CA	AA-	Aa2	AA-
Baltimore, MD	AA-	Aa3	(WD)
Chicago, IL	A+	Aa3	AA-
Washington, DC	A+	A1	AA-
St. Louis, MO	A+	A2	(NA)
San Diego, CA	A	A2	AA-
Cleveland, OH	A (lease)	A2	AA-
Philadelphia, PA	BBB	Baa1	A-
New Orleans, LA	BBB	Baa3	A-
Pittsburgh, PA	BBB	Baa1	A
Detroit, MI	**BB**	**Ba3**	**BB**

NA not available WD withdrawn

Source: U.S. Census Bureau, Statistical Abstract of the United States: 2012, Table 446.

Table 13
City of Detroit General Obligation Debt Ratings

	Unlimited Tax Bonds	Limited Tax Bonds
Moody's	Ba2	Ba3
Standard and Poor's	BB	BB
Fitch	BB	BB-

Source: City of Detroit Website, Finance Department, Debt Management Division (www.detroitmi.gov/DepartmentsandAgencies/Finance/DebtManagementDivision.aspx)

According to the city's website, Moody's and Fitch rate Detroit's unlimited tax bonds slightly higher than limited tax bonds (See **Table 13**).

Comparisons of debt loads among cities present challenges, however, because different cities are responsible for different combinations of services: the allocation of responsibilities between cities, counties, and states differs; some city governments include schools; and the use of special authorities for major services and infrastructure varies as well. Nonetheless, it is possible to compare the debt outstanding of the largest cities using the most recent data available from the U.S. Census Bureau (the comparison data are from 2006). (See **Table 14**.)

Table 14
City Government Expenditures and Outstanding Debt for the Largest Cities, 2006

City	Total Expenditures in Millions	Outstanding Debt in Millions	Debt as a Percent of Expenditures	Estimated Population in Thousands	Debt Per Capita
Jacksonville, FL	$3,474	$11,022	317.3%	795	$13,872
San Francisco, CA	6,908	8,738	126.5	744	11,744
New York, NY	82,454	85,234	103.4	8,214	10,376
Detroit, MI	**3,349**	**7,515**	**224.4**	**871**	**8,627**
Dallas, TX	2,713	8,557	315.4	1,233	6,940
Chicago, IL	7,622	15,862	208.1	2,833	5,598
Houston, TX	3,982	11,403	286.4	2,144	5,317
Indianapolis, IN	3,412	4,125	120.9	786	5,251
Phoenix, AZ	3,362	7,373	219.3	1,513	4,873
San Jose, CA	1,894	4,368	230.6	930	4,697
San Antonio, TX	3,625	6,055	167.0	1,297	4,670
Los Angeles, CA	12,315	15,723	127.7	3,849	4,085
Philadelphia, PA	6,745	5,825	86.4	1,448	4,022
Columbus, OH	1,152	1,703	147.8	733	2,323
San Diego, CA	2,431	2,795	115.0	1,257	2,224

Source: 2012 Statistical Abstract of the United States, Table 458; CRC calculations

Detroit Bonded Debt

The City of Detroit has borrowed money for a number of purposes, including to provide cash for operations, to construct and maintain infrastructure, and, as noted previously, to fund pensions. "Limited tax" bonds are repaid from the General Fund's general operating revenues; "unlimited tax" bonds are repaid from unlimited property tax levies (the debt service levy for unlimited tax bonds grew from 8.9157 mills in FY2010 to 9.5558 mills in FY2012), and "revenue" bonds are repaid from dedicated revenues such as water or sewerage charges.

The total amount of Detroit primary government debt (including pension obligation certificates and water and sewerage debt) outstanding at June 30, 2010 was $7.7 billion, or about $10,800 per capita using the 2010 population of 713,777.

The total amount of Detroit primary government debt (including pension obligation certificates and water and sewerage debt) outstanding at June 30, 2010 was $7.7 billion, or about $10,800 per capita using the 2010 population of 713,777. This compares with total primary government debt of $3.3 billion at June 30, 2001; $7.2 billion at June 30, 2005 after the sale of pension obligation certificates[9]; and $7.5 billion in the 2006 data in the table above (the difference in the 2006 estimated Detroit population of 871,121 and the 2010 census number of 713,777 accounts for the per capita differences).[10] Compared to other large U.S. cities, Detroit's debt per capita is very high.

Table 15 shows that at June 30, 2010, debt service requirements excluding the $1.5 billion of outstanding pension obligation debt that was described previously.

Excluding pension obligation certificates, general obligation debt backed by the full faith and credit of the city totaled $1.0 billion (about $1,400 per capita) with interest obligations of $469.3 mil-

[9] June 30, 2010 City of Detroit Comprehensive Annual Financial Report, page 199.

[10] June 30, 2010 City of Detroit Comprehensive Annual Financial Report, page 199.

Table 15
Debt Service Requirements 2011-2040
(Dollars in Millions)

	Principal	Interest	Other*	Total
Governmental Activities				
General Obligation Debt	$1,010.3	$467.7		$1,478.0
Revenue Bonds and Other	127.4	39.4		166.8
Business Activities				
Sewage Disposal	$2,987.5	$2,075.4	$274.0	$5,336.9
Water Fund	2,252.7	1,944.0	0.5	4,197.2
Transportation (G.O.)	6.3	1.6		7.9
Automobile Parking	39.1	7.3	24.1	70.5
Grand Total	$6,423.3	$4,535.4	$298.6	$11,257.3

* Hedging, derivatives, Net

Source: June 30, 2010 City of Detroit Comprehensive Annual Financial Report, pages 106-107 lion. Revenue bonds of the city's business enterprises totaled $5.3 billion. Sewerage bonds are payable solely from the net revenues of the sewer system; water bonds are payable solely from the net revenues of the water system.

As noted, limited tax debt paid from the operating revenues of the General Fund reduces the funding available for other municipal services. In 2010, Detroit sold $249.8 million of limited tax bonds payable from distributable state aid (revenues received from the state) to fund a portion of the accumulated and projected deficit. **Table 16** shows the city's limited tax debt service requirements, according to the prospectus for those bonds.

In FY2012, the $58.7 million in principal and interest due on this limited tax debt is 3.7 percent of the $1.6 billion total appropriations for general city agencies. It is more than the $53.9 million appropriated for the Public Lighting Department or the $53.9 mil-

Table 16
City of Detroit Limited Tax General Obligation Debt Service Schedule
(Dollars in Millions)

Fiscal Year Ending June 30	Debt Service 2010 Series Bonds	Other Limited Tax Debt Service	Total
2011	$14.1	$46.1	$60.2
2012	12.6	46.1	58.7
2013	12.6	52.5	65.1
2014	12.6	52.1	64.7
2015	18.9	32.6	51.5
2016	18.8	32.6	51.4
2017	18.8	9.3	28.1
2018	18.8	9.3	28.1
2019	18.8	9.3	28.1
2020	18.8	9.3	28.1
2021	18.9	9.7	28.6
2022	18.8	8.0	26.8
2023	18.8	7.9	26.7
2024	18.8	8.0	26.8
2025	18.8	8.0	26.8
2026	18.8		18.8
2027	18.8		18.8
2028	18.8		18.8
2029	18.8		18.8
2030	18.8		18.8
2031	18.8		18.8
2032	18.8		18.8
2033	18.8		18.8
2034	18.8		18.8
2035	18.8		18.8
2036	18.8		18.8
Total	$466.4	$387.1	$853.5

Source: Prospectus, Series 2010 Bonds, pages 7, A-44.

lion appropriated for the Detroit Workforce Development Department.

Voters must approve the sale of unlimited tax debt. This type of debt does not compete with general city services such as police and fire protection because it is repaid from the proceeds of a property tax levy that is set at a millage rate that is recalculated annually to generate sufficient cash to repay the principal and interest due that year. For FY2010, Detroit levied a debt service millage rate of 8.9157, which was in addition to the 19.952 operating millage rate. This was not the highest debt service rate imposed by a city in Michigan, but the River Rouge and Ecorse (Ecorse is operating under a state-appointed emergency manager) rates included judgment levies (See **Table 17**).

In FY2012, Detroit's debt service tax rate had increased to 9.5558 mills, reflecting in part the decline in taxable value.

Michigan's Home Rule Cities Act generally limits the net indebtedness of cities to ten percent of the assessed value of real and personal property in the city. At June 30, 2010, the city's debt limit was $1.2 billion and the outstanding net general obligation debt that was applicable to the limit was $919.7 million (75.46 percent of the legal limit). The city's legal debt margin, the amount of new debt that could be issued, was $299.1 million.[11] On December 16, 2010, the city issued $100.0 million of unlimited tax general obligation bonds for various capital projects. Those bonds begin to mature in 2014 and will fully mature in 2035.

As Detroit's fiscal situation deteriorates, questions may arise as to the city's ability to service its debt. As noted, a relatively small share of the city's bonded debt is backed by the full faith and credit of the city, while the great majority is guaranteed by designated, dedicated revenues. If all parties agree, debt can be renegotiated, which is what usually happens in a default situation. Under PA 4 of 2011, an emergency manager has the authority to "Enter into agreements with creditors or other persons or entities to restructure debt on terms, at rates of interest, and with security as shall be agreed among the parties, subject to approval by the state treasurer." Another possible remedy for inability to meet debt obligations is bankruptcy, in which municipalities can restructure and reorganize assets and debts. Under PA 4, the state appointed financial manager would be required to obtain permission from the governor for the local government to file under Chapter 9, Title 11 of the United States Code and would act on the local government's behalf in bankruptcy proceedings.

Table 17
Michigan Cities: Debt Service Rates, FY2010

City	Debt Service Millage Rate
River Rouge	18.97
Ecorse	10.69
Inkster	10.33
Detroit	**8.92**
Flint	6.71
Sylvan Lake	5.97
Huntington Woods	5.21
Clarkston	4.94
Ypsilanti	4.39
Orchard Lake	4.72
Center Line	4.91
Eaton Rapids	4.40
Cheboygan	4.10

Source: Michigan Department of Treasury

[11] June 30, 2010 City of Detroit Comprehensive Annual Financial Report, page 204.

Other Future Obligations

The city estimates that its long-term liabilities include accrued compensated absences for employees ($123.0 million), accrued worker's compensation ($66.2 million), claims and judgments ($93.0 million), and accrued pollution remediation (0.4 million).[12] Detroit has used Section 108 loans from the federal government for revitalization projects; the city has pledged $89.5 million of future Block Grant funds to repay these loans. Several other loans, including one to the DDA, total $37.9 million. The city has commitments for future construction activity that totaled $78.2 million at June 30, 2010. Future commitments for operating leases for equipment totaled $130.3 million at June 30, 2010.[13] All of these obligations total $618.5 million.

As noted, under PA 4 of 2011 an emergency manager may reject, modify, or terminate one or more terms and conditions of an existing contract.

Conclusions

While the various debts and future obligations of all funds of the city government total considerably more than $19,000 for every resident of the city, a large proportion of the outstanding debt will be paid by nonresident customers served by the Detroit Water and Sewer Department (the Sewage Disposal Fund retired $34.8 million of revenue bonds in FY2010; the Water Fund retired $33.6 million of revenue bonds that year). Furthermore, the total future liability includes a substantial amount that is funded on a pay-as-you-go basis, for which there is no penalty for having an UAAL, and which may be renegotiated or otherwise reduced. The City of Detroit has so far managed to either meet minimum obligations when those obligations were due, or to renegotiate the obligation to enable the debt to be sustained.

The General Fund subsidizes the Transportation Department, and the relatively small amount of Transportation bonded debt is the general obligation of the city. The $209.1 million of principal and interest on pension funding certificates attributable to the Transportation Fund, the growing UAAL in the pension fund, and the considerable amount of UAAL for other post employment benefits associated with Transportation Fund employees present substantial impediments to the realignment of that system.

Detroit, like other local governments in Michigan, is struggling to provide essential services with declining revenues. The general city's below investment grade bond rating and a certain unease with municipal debt in the markets may well increase the cost of borrowing at the same time that the general city's cash flow problems are increasing. Detroit issued $249.8 million of limited tax fiscal stabilization bonds in March, 2010, enabling the city to reduce short term borrowing, but predictions are that cash flow will again be severely stressed early in 2012. (Mayor Dave Bing has stated that the city will run out of cash in April if union concessions and other cost savings measures are not implemented.) It remains to be seen whether city officials, unions, contractors and other affected entities can develop and implement a strategy to restore the financial viability of the city, or whether the state, acting under PA 4 of 2011 or other authority, will be forced to intervene.

[12] June 30, 2010 City of Detroit Comprehensive Annual Financial Report, page 92.

[13] June 30, 2010 City of Detroit Comprehensive Annual Financial Report, page 125.

Addendum

The following information from the City of Detroit's $3.1 billion budget for FY2012 is provided to help put the numbers in this report in perspective.

Taxable value of all real and personal property on the ad valorem tax roll: $8.3 billion.

Table 18
City of Detroit Budget Overview, FY2012
(Dollars in Millions)

Budgeted Appropriations		
Police Department	$414.8	
Fire Department	183.4	
Department of Public Works	114.4	
Prior Years Deficit	55.2	
All Other General City Departments	814.7	
Total General City Agencies		$1,582.5
General City Debt Service		77.7
Water Fund	$686.0	
Sewerage Fund	518.7	
Transportation Department	149.4	
Other Enterprise Agencies	94.0	
Total Enterprise Agencies		1,448.1
Total Appropriations		$3,108.3
Budgeted Major Revenues		
Municipal Income Tax	$250.0	
Net Property Tax	204.8	
Casino Wagering Tax	174.8	
Other Casino Payments	40.1	
Utility Users' Excise Tax	42.0	
Solid Waste Fees	47.9	
Sale of Electricity and Steam	60.7	
State Revenue Sharing (General Fund)	165.6	
Other State Grants	140.2	
Federal Grants	267.0	
Revenue from Enterprise Agency Operations	983.6	
Sale of Water Revenue Bonds	300.0	
All Other Revenues	431.6	
Total Revenues		$3,108.3