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EMERGENCY FISCAL MANAGERS FOR MUNICIPALITIES

**Senate Bill 771 (Substitute H-1)
First Analysis (12-9-03)**

**Sponsor: Sen. Robert Emerson
House Committee: Local Government
and Urban Policy
Senate Committee: Local, Urban and
State Affairs**

THE APPARENT PROBLEM:

Under Michigan law, a local unit of government cannot declare bankruptcy, a prohibition that exists in order to protect the creditworthiness of the state as a whole. Instead, the legislature passed the Local Government Fiscal Responsibility Act—Public Act 72 of 1990—which enables the state treasurer to intervene when local units are in financial trouble. Following a review done by a review board, an emergency financial manager can be appointed. The law confers the combined power of mayor and city council upon financial managers, allowing them to unilaterally take action—including privatization of city services—to balance the books in troubled local governments. The appointment of an emergency financial manager is triggered when a city fails to provide an annual financial report or audit that conforms with the minimum procedures and standards of the state treasurer, as required under the Uniform Budgeting and Accounting Act which defines budgeting and accounting standards.

Three municipal governments in Michigan have experienced financial crises in the past decade—Flint, Hamtramck, and Highland Park—and the state treasurer has appointed an emergency financial manager in each jurisdiction. The first city in crisis, Hamtramck, faced a \$2.4 million debt, and Louis Schimmel was appointed emergency financial manager in November 2000. After nearly three years, the City of Hamtramck will soon regain full authority over its finances, a return to local control that has recently been approved by the state's Emergency Loan Board. The second city in crisis, Highland Park, was delinquent in making a \$525,000 payment to the Michigan Employee Retirement System as required by law, as well as attempting to issue a \$3.4 million bond to cover a deficit, when Ramona Henderson Pearson was appointed emergency financial manager in December 2000, an appointment that was delayed for several months

because it was enjoined in Wayne County Circuit Court. In the summer of 2002, the City of Flint faced a \$26 million deficit, and Ed Kurtz was appointed emergency financial manager.

In all of these financial crises, the appointed emergency financial managers have reduced or eliminated the salary of the mayor and city council, in accord with the authority granted to them under the law. However, when the manager reduced the salaries of the officials in Highland Park, her action was challenged in judicial proceedings. Initially, a state administrative law judge upheld the emergency manager's action, however, a local circuit court judge reversed that ruling, and found instead that the emergency manager had exceeded her authority. The ruling was not appealed. Subsequently, in the City of Flint, the emergency financial manager reduced the annual pay of the mayor from \$110,000 to \$24,000, as well as the pay of the city council members from \$24,000 to \$18,000. The Flint officials also have appealed their cut in their pay.

In order to clarify that an emergency financial manager has the authority to eliminate or reduce an official's salary during a financial crisis, legislation has been introduced. Further, to settle any question of legal wrong-doing that may have precipitated the financial crisis, the legislation would require an emergency financial manager to report suspected criminal acts to the state attorney general, as well as to the local prosecutor.

THE CONTENT OF THE BILL:

The bill would amend the Local Government Fiscal Responsibility Act to give an emergency financial manager additional powers, including the authority to reduce, suspend, or eliminate the salary or other compensation of members of the governing body of a

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local unit of government during a financial emergency.

If an emergency financial manager had reduced, suspended, or eliminated the salary or other compensation of the chief administrative officer and members of the governing body of a local unit before the bill's effective date, the reduction, suspension, or elimination would be valid to the same extent had it occurred after the bill's effective date. The bill specifies that these provisions would not authorize a manager to impair vested retirement benefits.

Currently, an emergency financial manager may exercise the authority and responsibilities affecting the financial condition of the local unit, as provided in various statutes cited in the act that govern different types of local units. The bill specifies that the manager could exercise the authority and responsibilities of the local unit's chief administrative officer and governing body concerning the adoption, amendment, and enforcement of ordinances or resolutions affecting the financial condition of the local unit as provided in the statutes cited.

Under the act, an emergency financial manager may consolidate departments or transfer functions from one department to another and appoint, supervise, and, at his or her discretion, remove heads of departments other than elected officials, notwithstanding the provisions of any charter to the contrary. However, the emergency financial manager could not remove the clerk of the unit of local government, or any ombudsman position in the unit of local government.

The bill specifies that if a financial emergency existed under the Local Government Fiscal Responsibility Act, then the emergency financial manager would be required to make a determination as to whether possible criminal conduct contributed to the financial emergency. If the manager determined that there was reason to believe that criminal conduct had occurred, the manager would be required to refer the matter to the attorney general and to the local prosecuting attorney for investigation. Under the bill, this determination would be required to be made by one of the following dates, whichever was later: a) within 90 days after the effective date of the amendatory act that added this subsection; or b) within 180 days after the date the emergency financial manager was appointed.

Finally, the bill specifies that not later than 90 days after the completion of the emergency financial manager's term, the governing body of the unit of

local government would be required to review any ordinance implemented by the emergency financial manager during his or her term, except any ordinance enacted to assure the payment of principal and interest on bonds.

MCL 141.1221

HOUSE COMMITTEE ACTION:

The members of the House Committee on Local Government and Urban Policy adopted an H-1 Substitute for Senate Bill 771. The substitute differs from the Senate-passed version of the bill in five ways:

First, an emergency financial manager would be able to consolidate departments of the unit of local government "*notwithstanding the provisions of any charter to the contrary*";

Second, an emergency financial manager *could not* remove the clerk of the unit of local government, or the ombudsman position in the unit of local government;

Third, an emergency financial manager could enter into agreements with other units of local government—but not the state (as specified in the Senate-passed version)—for the provision of services;

Fourth, in the H-1 substitute, an emergency financial manager could reduce, suspend, or eliminate the salary, or other compensation of members of the governing body of the unit of local government during the financial emergency (whereas in the Senate-passed version the manager could also reduce, suspend, or eliminate the salary of the chief administrative officer); and,

Fifth, not later than 90 days after the completion of the emergency financial manager's term, the governing body of the unit of local government would be required to review any ordinance implemented by the emergency financial manager during his or her term, *except* any ordinance enacted to assure the payment of principal and interest on bonds.

FISCAL IMPLICATIONS:

The House Fiscal Agency notes that as written, the bill should have little direct state or local fiscal impact. (12-2-03)

ARGUMENTS:

For:

Proponents of the legislation argue that an emergency financial manager should have the legal authority to reduce the salaries of elected officials, in order to address the financial crisis of the local unit of government whose fiscal affairs must be corrected. For example, in two cities where emergency financial managers have been appointed, the salary of the mayor has exceeded \$100,000 (even though the cities also had city managers). Since the mayor’s duties are substantially curtailed as the emergency manager appointed by the Department of Treasury takes charge, the mayor’s salary also should be reduced or eliminated. Currently the emergency manager’s legal authority to alter the salaries of elected officials is not clearly stated in the law. This bill would make the manager’s authority explicit and clear.

Proponents also argue that when an emergency manager uncovers evidence of possible criminal wrongdoing while investigating the reasons for the fiscal crisis, he or she should be required to report such behavior to the local law enforcement officials, as well as to the state attorney general. This legislation would require the emergency manager to do so.

Response:

In its current form, the bill would not allow the emergency financial manager to reduce, suspend, or eliminate the compensation of the local unit’s “chief administrative officer” (as the Senate-passed bill would have allowed). In the case of a city, that term can refer to a city manager or, if there is no city manager, to the mayor of the city. Does this mean that when there is no city manager, the mayor’s salary can be reduced, suspended, or eliminated? Is the mayor included in the term “governing body”? Is this an area that needs clarification?

Against:

Opponents of this legislation argue that the authority of officials who are duly elected by the citizens of a community—and whose responsibilities are often described in the local charters of the governmental units in which they serve—should not be carelessly or completely abridged by a temporary manager assigned by the state to act as both executive and legislature for a brief time. To block or suspend all of the legal responsibilities of the elected officials means that the citizens who elected them bear the burden of taxation without representation, and that is not the American way.

Opponents also argue that the act needs a complete and thorough overhaul, in part because the law does not now provide for the emergency financial manager’s leave-taking once the fiscal crisis has passed. Absent an exit strategy for the short-term emergency manager, these appointed officials can overstay the need for them, holding absolute power much longer than is necessary, unaccountable to anyone.

POSITIONS:

The Department of Treasury supports the bill. (12-8-03)

The Flint Branch of the NAACP testified in opposition to the bill. (12-2-03)

A representative for the Mayor of the City of Flint testified in opposition to the bill. (12-2-03)

The Genesee County Prosecutor testified in opposition to the bill. (12-2-03)

The Flint City Council opposes the bill. (12-8-03)

Analyst: J. Hunault

■This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.