



STATE OF MICHIGAN
DEPARTMENT OF TREASURY
LANSING

RICK SNYDER
GOVERNOR

ANDY DILLON
STATE TREASURER

DATE: May 23, 2013

TO: Governor Snyder

FROM: Hamtramck Financial Review Team:
Max Chiddister
Frederick Headen
Edward B. Koryzno, Jr.
Eric Lupher
Doug Ringler

SUBJECT: Report of the Hamtramck Financial Review Team

On April 17th and 30th and May 2nd, and 10th, Hamtramck Financial Review Team members met and reviewed information relevant to the financial condition of the City of Hamtramck. Based upon that review, the Review Team concludes, in accordance with Section 5(4)(b) of Public Act 436 of 2012, the Local Financial Stability and Choice Act, that a financial emergency exists within the City of Hamtramck.

I. Background

A. Preliminary Review¹

On February 11th through March 13th, 2013, the Department of Treasury conducted a preliminary review of the finances of the City of Hamtramck to determine whether or not a serious financial problem existed. The preliminary review of the City of Hamtramck resulted from the conditions enumerated in subdivision (a) and (j) of Section 12(1) having occurred within the City.² The preliminary review found, or confirmed, the following:

- City officials had adopted budgets, or budget amendments, or both, that do not comply with Public Act 2 of 1968, the Uniform Budgeting and Accounting Act. For example, for the 2012 fiscal

¹ The preliminary review was conducted pursuant to former Public Act 72 of 1990, the Local Government Fiscal Responsibility Act, which then was in effect. Public Act 72 subsequently was repealed by Public Act 436 of 2012, the Local Financial Stability and Choice Act, which took effect on March 28, 2013.

² Subsection (a) provided that “[t]he governing body or the chief administrative officer of a local government requests a preliminary review under this article. The request shall be in writing and shall identify the existing financial conditions that make the request necessary.” Subsection (j) provided that “[t]he local government has violated a requirement of sections 17 to 20 of the uniform budgeting and accounting act, 1968 PA 2, MCL 141.437 to 141.440, and the state treasurer has forwarded a report of this violation to the attorney general.”

year, City officials adopted a General Fund budget that had a net negative \$1.7 million change in fund balance due primarily to a \$1 million over estimation of property tax revenues and expenditures exceeding budgeted revenues for fire services by \$427,360 and for public works by \$457,828. This same budget resulted in an actual unrestricted General Fund deficit of \$753,733. Similarly, City officials amended the 2013 fiscal year budget in November of 2012, without addressing an operating deficit of \$2.7 million. In short, City officials made little effort to address a revenue shortfall by reducing expenditures as required by Public Act 2 of 1968.

- Subsequently, officials submitted a deficit elimination plan that was deemed unacceptable by the Department of Treasury. For the 2013 fiscal year, the deficit elimination plan included significant revenue enhancements, amounting to \$781,231, and \$241,500 in expenditure reductions. Yet, City officials provided no evidence that the revenue enhancements were realistic or that the expenditure reductions could be made. However, even if the revenue enhancements and expenditure reductions were fully realized, City officials projected expenditures to exceed revenues by over \$1.7 million. In other words, the deficit elimination plan failed to provide any reasonable assurance that the City is adequately addressing its structural deficit.

Furthermore, while the request for a preliminary review by City officials noted an inability to achieve concessions from employee unions, the deficit elimination plan included \$2.5 million in labor concessions for the 2015 fiscal year when existing labor contracts expire at the end of the 2014 fiscal year. However, the deficit elimination plan provided no detail concerning the probability of attaining the concessions or how the City anticipates achieving them.

- City officials utilized assets from other City funds to increase cash flow in the General Fund. Among the more significant transactions were \$110,206 from the Water and Sewer Fund and \$500,000 from the Local Streets Fund. Borrowing from other funds is indicative of cash flow issues.

As indicated in **Table 1** on the next page, for the City's 2009 fiscal year, General Fund revenues exceeded General Fund expenditures by more than \$1.3 million. However, in the 2010 fiscal year, the opposite occurred, with expenditures exceeding revenues by almost \$1.2 million. The 2011 fiscal year realized an increase in property taxes because of a one-time payment from the City of Detroit and an increase in fund balance because of a \$2 million transfer from the City's Budget Stabilization Fund.

However, the overall trend of the City's financial condition reflected a decline in revenues during this period. Had the City paid attention to the decline in property tax revenue, and made the necessary cuts in fiscal year 2011, it could have potentially avoided a General Fund deficit while preserving the one-time payment and Budget Stabilization Fund transfer. However, failing to make reductions in expenditures created overall fund deficits.

Table 1
General Fund Revenues, Expenditures,
and Change in Fund Balance

	2009	2010	2011	2012	2103 (Projected)
Revenues	\$19,442,075	\$15,950,187	\$17,308,211	\$14,827,148	\$16,097,514
Expenditures	\$18,056,312	\$17,141,107	\$17,649,427	\$18,130,533	\$17,822,122
Current Surplus/ (Deficit)	<u>\$1,385,763</u>	<u>(\$1,190,920)</u>	<u>(\$341,216)</u>	<u>(\$3,303,385)</u>	<u>(\$1,724,608)</u>
Other Financing Sources			\$2,000,000		
Beginning Fund Balance	<u>\$867,393</u>	<u>\$2,253,156</u>	<u>\$1,062,236</u>	<u>\$2,721,020</u>	<u>(\$582,365)</u>
Ending Fund Balance	<u>\$2,253,156</u>	<u>\$1,062,236</u>	<u>\$2,721,020</u>	<u>(\$582,365)</u>	<u>(\$2,306,973)</u>
Ending Fund Balance (Unassigned/Unreserved)	\$2,162,215	\$959,486	\$ 2,519,246	(\$753,733)	NA

Source: City of Hamtramck Annual Financial Audits, 2009 through 2012

- City officials had delayed making approximately \$2.2 million in required pension contributions in order to manage cash flow. At the time of the preliminary review, it was anticipated that the City could deplete its cash by April 2013, unless City officials continued to forego required pension contributions, thus increasing the \$2.2 million arrearage by an estimated \$295,000 for each additional month of delayed payments. It was anticipated that City officials also would need to delay repayment of \$500,000 to the Local Streets Fund and other accounts payable.
- The unfunded liabilities of the City’s pension and other post-employment benefits (OPEB) posed significant obstacles to its long-term fiscal health. An actuarial evaluation based on data from the 2011 calendar year (the latest then available) indicated the pension plan had \$98.4 million in actuarial accrued liabilities, but only \$55.8 million in pension assets. Therefore, the pension plan had an unfunded actuarial accrued liability of \$42.5 million (i.e., a funding ratio of only 56.8 percent). The OPEB liability exceeded \$47 million. A funded ratio was not available since there were no plan assets because City officials have adopted a “pay as you go” basis for financing. Between 2010 and 2011, the pension liability increased by more than \$3.5 million and the OPEB liability has increased by more than \$16 million since 2009.
- While the Water and Sewer Fund had a significant balance of net assets, a sizeable shift had taken

place related to its operating income. As reflected in **Table 2**, each fiscal year from 2009 to 2011, the City saw a positive operating income. Fiscal year 2010 even reflected an excess of \$1.1 million. However, the audited financial statements for the 2012 fiscal year reflect an operating loss of \$409,999, which was the direct result of higher charges the City was obligated to remit to the City of Detroit for its water supply. Water and Sewer rates have not kept pace with these increases even though the City of Hamtramck increased rates in 2011 by 9.1 percent for water services and by 11 percent for sewer services.

Table 2
Water and Sewer Fund Revenues, Expenditures,
and Change in Net Assets

	2009	2010	2011	2012
Revenues	\$4,733,048	\$5,488,325	\$5,998,073	\$5,169,627
Expenditures	\$4,398,404	\$4,361,153	\$5,834,743	\$5,579,626
Operating Income	<u>\$334,644</u>	<u>\$1,127,172</u>	<u>\$163,330</u>	<u>(\$409,999)</u>
Non-Operating Revenue/ (Expenses)	(\$5,344)	\$300	\$5,321	\$43,531
Beginning Net Assets	<u>\$4,249,508</u>	<u>\$4,578,808</u>	<u>\$5,706,280</u>	<u>\$5,874,931</u>
Ending Net Assets	<u>\$4,578,808</u>	<u>\$5,706,280</u>	<u>\$5,874,931</u>	<u>\$5,508,463</u>

Source: City of Hamtramck Annual Financial Audits, 2009 through 2012

Based upon the foregoing preliminary review, the State Treasurer concluded, and reported to the Governor on March 13, 2013, that a serious financial problem existed in the City of Hamtramck and recommended the appointment of a financial review team.

B. Review Team Findings

On April 17, 2013, the Governor appointed a five-member Financial Review Team. The Review Team convened on April 24th and 30th, and May 2nd, and 10th, 2013.

1. Conditions Indicative of a Financial Emergency

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

- According to the City’s 2012 fiscal year financial audit, the ending balance in the General Fund decreased from \$2,721,020 as of June 30, 2011 to a negative \$582,365 as of June 30, 2012. This one-year negative net change in fund balance of \$3,303,385 resulted from an operating deficit (i.e., expenditures in excess of revenues) of the same amount.
- As summarized in **Table 3**, financial audit reports for the City for its last three fiscal years reflect notable variances between General Fund revenues and expenditures, as initially budgeted and as amended, versus General Fund revenues and expenditures actually realized. In all three of the years in question, General Fund revenues were overestimated, substantially so in fiscal years 2010 and 2012. In none of the three years in question did General Fund revenues exceed expenditures. These significant variances, in concert with an inability of City officials to accurately monitor revenues and expenditures throughout a given fiscal year and to properly amend City budgets accordingly, rendered the adopted budgets, and in many instances the amended budgets, effectively meaningless as a financial management tool.

Table 3

General Fund Revenues as Initially Budgeted, Amended, and Actual

	<u>2009-10</u>	<u>%</u>	<u>2010-11</u>	<u>%</u>	<u>2011-12</u>	<u>%</u>
<u>Revenues</u>						
Budgeted	\$19,002,132		\$16,903,680		\$16,135,878	
Amended	\$19,121,682		\$18,003,680		\$16,135,878	
Actual	<u>\$16,082,068</u>		<u>\$17,308,211</u>		<u>\$14,827,148</u>	
Variance	(\$3,039,614)	(15.90)	(\$695,469)	(3.86)	(\$1,308,730)	(8.11)
<u>Expenditures</u>						
Budgeted	\$18,198,234		\$17,532,423		\$18,234,578	
Amended	\$18,322,337		\$18,121,411		\$17,978,019	
Actual	<u>\$17,272,988</u>		<u>\$17,649,427</u>		<u>\$18,130,533</u>	
Variance	\$1,049,349	5.72	\$471,984	2.60	(\$152,514)	(0.85)

Source: Annual Financial Audits

- As of the date of submission of this Review Team report, City officials had not filed with the Michigan Department of Treasury a deficit elimination plan that is sufficient for certification. The proposed deficit elimination plan submitted by City official includes significant revenue enhancements (e.g., increased license and permit revenue, a 13 percent increase in City Income Tax revenues, and a 35 percent increase in fines and forfeitures revenues) as well as expenditure reductions. However, City officials provided no evidence that the proposed revenue enhancements were realistic or that the expenditure reductions would be made. Furthermore, even if the proposed revenue enhancements and expenditure reductions were to be fully achieved, City officials projected expenditures still would exceed available revenues by more than \$1.7 million. The filing of an approvable deficit elimination plan is required by State law.³

2. Review Team Meetings

On April 24, 2013, Review Team members Frederick Headen, Edward B. Koryzno, Jr., Eric Lupher, Doug Ringler, and Max Chiddister (by conference telephone), met with Cary Vaughn, Audit Manager, Local Audit and Finance Division, Bureau of Local Government Services; and with Surender Gupta, Anil Sakhuja, and James D. Wilde II, of the certified public accounting firm Alan C. Young & Associates.

On April 30, 2013, Review Team members Max Chiddister, Frederick Headen, Edward B. Koryzno, Jr., Eric Lupher, and Doug Ringler conducted a series of meetings in the City of Hamtramck with Karen Majewski, Mayor; Kyle Tertzag, Acting City Manager; Kathy Angerer, Assistant City Manager; Carl Johnson (Controller) and Carolyn Lorenz, of Plante and Moran; Steve Smiscik, President, Hamtramck Ranking Police Officers Associates; Andy Mileski, Vice President, Hamtramck Ranking Police Officers Association; David Cornwell, President, Hamtramck Fraternal Order of Police; Neil Egan, Vice President, Hamtramck Fraternal Order of Police; Mathew Wood, Secretary-Treasurer, Hamtramck Fraternal Order of Police; Brian Misiak, Hamtramck Fraternal

³ Section 21(2) of Public Act 140 of 1971, the Glenn Steil State Revenue Sharing Act of 1971, provides, in part, as follows:

For a fiscal year of a unit of local government ending on or after October 1, 1980 or any year thereafter, if a local unit of government ends its fiscal year in a deficit condition, the local unit of government shall formulate and file a financial plan within 90 days after the beginning of the fiscal year to correct this condition. Upon request of a local unit of government the department of treasury may assist that local unit in the formulation of the financial plan to correct the deficit condition. The local unit of government shall file the financial plan with the department of treasury for evaluation and certification that the plan ensures that the deficit condition is corrected.

Furthermore, one of the conditions for qualified status under Section 303(3)(m) of Public Act 34 of 2001, the Revised Municipal Finance Act, is that a “municipality did not end the immediately preceding fiscal year with a deficit in any fund, *unless* the municipality has filed a financial plan to correct that deficit condition that is acceptable to the department” [of Treasury]. Emphasis supplied.

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Order of Police; Max Garbarino, Police Chief; Matthew Wyszczelski, President, Hamtramck Firefighters Association; Justin Corsi, First Vice President, Hamtramck Firefighters Association; Andy Capo, Second Vice President, Hamtramck Firefighters Association; Michael Young, Secretary, Hamtramck Firefighters Association; Steve Brummer, Treasurer, Hamtramck Firefighters Association; and Paul Wilk, Fire Chief.

On May 2, 2013, Review Team members Max Chiddister, Frederick Headen, Edward B. Koryzno, Jr., Eric Lupher, and Doug Ringler conducted a series of meetings in the City of Hamtramck with Mohammed Hassan, Anam Miah, Abdul Algazali, Tom Jankowski, Cathie Gordon, and Robert Zwolak, Councilmembers; Michael Wilk, City Treasurer; Sandra Peavley, President AFSCME Local 666; Robyn Price, Staff Representative, AFSCME Council 25; Paul Paruk, Chief Judge, 31st District Court; and Margaret Scanio, Human Resources Director.

Also, on May 2, 2013, Review Team members Max Chiddister, Frederick Headen, Edward B. Koryzno, Jr., Eric Lupher, and Doug Ringler conducted a public information meeting in the City of Hamtramck pursuant to Section 5(2) of the Act. Review Team members discussed with City residents in attendance the status of the City's financial conditions, indicated the City officials and union officials with whom the Review Team had met, and received comments from a number of City residents.

3. Other Considerations

Previous Financial Emergency. The City of Hamtramck previously was subject to emergency financial management by this State pursuant to former Public Act 72 of 1990, the Local Government Fiscal Responsibility Act. On August 3, 2000, City officials executed a consent agreement with the Michigan Department of Treasury. However, City officials promptly failed to abide by the terms of that agreement and, as a result, an Emergency Financial Manager was appointed on November 16, 2000.

The Emergency Financial Manager resigned on February 23, 2006, after successfully concluding his assignment; the budget he had adopted for that fiscal year ended in surplus. Because City officials subsequently achieved certain benchmarks, including ending the 2007 fiscal year without a deficit, the City was released from emergency financial management pursuant to Executive Order 2007-45, on November 30, 2007.

Present Financial Emergency. The Review Team found it noteworthy that there was essentially unanimous acknowledgement from every City and union official with whom the Review Team met that a financial emergency exists within the City of Hamtramck. Likewise, there was essentially unanimous acknowledgement that the economic conditions which contributed to the financial emergency were neither precipitous nor unforeseen. In other words, it appears that the City's worsening financial condition was obvious to City officials, but that they were either unwilling or incapable of taking resolute action to address the matter.

During the course of our discussions with various individuals, two key themes emerged as contributing factors to the inability of City officials to address the City's decaying financial condition: frequent turnover in the City Manager position and significant dysfunction within the City Council. Neither of these deficiencies is, in itself financial in nature, but each appears to have contributed to the City's financial emergency.

First, we address the City Manager position. Since the City was released from emergency financial management in November 2007, it has had six different individuals serve in the City Manager position, in either a permanent or acting capacity. In fact, five of those individuals have served within approximately the last 12 months. Many City officials interviewed by the Review Team indicated that the frequent turnover in this key managerial and administrative position resulted in an ever-changing strategic direction within the City which, in turn, had a profound impact upon day-to-day City operations.

It also was noted by several City officials that the frequent turnover in the City Manager position posed a considerable challenge to City staff seeking to adapt to changes in management styles and resulted in ineffective communication. For example, City and union officials expressed considerable differences of opinions regarding the amount of labor concession that had been requested and the amount of such concession that had been offered in response.

Second, we address the dysfunction within the City Council. While several City Councilmembers we interviewed seemed individually knowledgeable regarding the City's financial condition, the members of that body seemed unable to function collectively in a coherent manner. City Councilmembers themselves indicated that financial leadership by that body has been demonstrated only in the breach. With that assessment, we concur. Furthermore, we include the Mayor in our assessment. While the Mayor is separately elected, the office is so inextricably linked to the City Council as to be part of the local governing body. For example, the Mayor attends City Council meetings and is responsible for presiding at them.

The Review Team was informed that City Council meetings are chaotic, protracted, and produce little in the way of tangible results. In such an environment, rational financial management is not likely to be forthcoming. Illustrative of this point is the fact that when Review Team members inquired of City Councilmembers regarding a proposed plan to address the City's financial condition, the response from most City Councilmembers was that they intended to request an emergency manager.

Indeed, the prevailing attitude among several City Councilmembers was that an emergency manager would quickly remedy the City's financial condition (by which they meant that an emergency manager would relieve them of the financial burdens of collective bargaining agreements into which they now believe they improvidently entered) and that just as quickly State officials would remove the City from receivership and return it to local control. Certainly, some of the collective

bargaining agreements would benefit from an independent review.⁴

However, even if the City's financial condition is successfully resolved, there will remain the matter of its operational and managerial dysfunction. Therefore, if a financial emergency is determined to exist within the City, if that determination subsequently is confirmed, and if City officials then select the statutory option of an emergency manager, before the City is removed from receivership, serious consideration should be given to appointing a Receivership Transition Advisory Board pursuant to Section 23 of the Act, as well as imposing the conditions authorized by Section 22(4) of the Act.⁵

C. Conclusion

Based upon the foregoing information, meetings, and review, the Review Team confirms the findings of the preliminary review, and concludes that a financial emergency exists within the City of Hamtramck.

⁴ Several of those collective bargaining agreements provide for comparatively generous compensation given the City's geographic area and population. The City of Hamtramck consists of 2.09 square miles and has a population of 22,423 (based on the 2010 decennial census), while the City of Flint, for example, consists of 34.06 square miles and has a population of 102,436. Nevertheless, the maximum salary for a police lieutenant in the City of Hamtramck is \$77,705 compared to \$63,447 in the City of Flint, while the maximum salary for a police sergeant in the City of Hamtramck is \$70,641 compared to \$56,309 in the City of Flint.

Similarly, the existing collective bargaining agreement with the Hamtramck Firefighters Association, which expires on June 30, 2014, provides for a 16 percent increase in wages over the term of the agreement. Under the agreement, firefighters received a four percent increase on July 1, 2009; a three percent increase on July 1, 2010; a three percent increase on July 1, 2011; a three percent increase on July 1, 2012; and are scheduled to receive a three percent increase on July 1, 2013.

Finally, the collective bargaining agreements with both the Hamtramck Ranking Police Officers Association and the Hamtramck Fraternal Order of Police allow for up to 32 hours of overtime per pay period for police personnel to write traffic tickets for purposes of a traffic safety program. It might be argued that writing traffic tickets, when appropriate, is a routine part of daily police work that should be performed during a regular shift as opposed to on an overtime basis. Given the City's perilous financial condition, the justification for collective bargaining agreement provisions that reward or incentivize overtime is not readily apparent.

⁵ Section 22(4) of the Act provides as follows:

(4) Before removing a local government from receivership, the governor may impose 1 or more of the following conditions on the local government:

(a) The implementation of financial best practices within the local government.

(b) The adoption of a model charter or model charter provisions.

(c) Pursue financial or managerial training to ensure that official responsibilities are properly discharged.

II. Section 5(3) Requirements

Section 5(3) of the Act requires that this report include the existence or an indication of the likely occurrence of any of the conditions set forth in subdivisions (a) through (m).⁶ The conditions in subdivisions (b) (iii), (f), (j), (k) of Section 5(3) exist or are likely to occur, as follows:

⁶ Subdivisions (a) through (m) of Section 5(3) of the Act provide as follows:

(a) A default in the payment of principal or interest upon bonded obligations, notes, or other municipal securities for which no funds or insufficient funds are on hand and, if required, segregated in a special trust fund.

(b) Failure for a period of 30 days or more beyond the due date to transfer 1 or more of the following to the appropriate agency:

(i) Taxes withheld on the income of employees.

(ii) For a municipal government, taxes collected by the municipal government as agent for another governmental unit, school district, or other entity or taxing authority.

(iii) Any contribution required by a pension, retirement, or benefit plan.

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

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

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

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

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

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

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

(j) Existence of a structural operating deficit.

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

- City officials had, as of the time of the preliminary review, delayed making a number of required monthly pension contributions to the Municipal Employees Retirement System of Michigan in order to manage cash flow. As of the time this Review Team report was finalized, the amount of unremitted pension contributions was approximately \$1.6 million for the months of September, November, and December 2012, and January, February, and March 2013. (Section 5(3)(b) (iii).)⁷
- The projected General Fund deficit of \$3.3 million as of June 30, 2013, exceeds 5 percent of the \$16,070,514 in General Fund revenues which the City has budgeted for the 2013 fiscal year as reported in the fiscal year 2013 Executive Budget. (Section 5(3)(f).)
- A structural operating deficit has existed in the City's General Fund during the last three fiscal years in the amount of \$1,190,920 in fiscal year 2010, \$341,216 in fiscal year 2011, and \$3,303,385 in fiscal year 2012. (Section 5(3)(j).)

III. Review Team Report Transmittal Requirements

Section 5(3) of the Act also requires that a copy of this report be transmitted to Hamtramck Mayor Karen Majewski, Hamtramck City Councilmembers, the Speaker of the House of Representatives, the Senate Majority Leader, and each State Senator and Representative who represents the City of Hamtramck.

cc: Karen Majewski, Mayor
Hamtramck City Councilmembers
James Bolger, Speaker of the House of Representatives
Randy Richardville, Senate Majority Leader
Bert Johnson, Michigan Senator
Rose Mary Robinson, Michigan Representative

(l) The likelihood that the local government is or will be unable to pay its obligations within 60 days after the date of the review team's reporting its findings to the governor.

(m) Any other facts and circumstances indicative of local government financial emergency.

⁷ It should be noted a City official expressed to the Review Team the view that the unremitted pension contributions in question were not actually due to the Municipal Employees Retirement System of Michigan until the end of the City's fiscal year (i.e., by June 30). This view was incorrect. Officials at the Municipal Employees Retirement System of Michigan indicated that member municipalities are required to remit contributions on a monthly basis and are assessed a penalty upon contributions that are more than 60 days in arrears. As a result, the City of Hamtramck has been assessed approximately \$1,200 in penalties to date.