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PRIVILEGED AND CONFIDENTIAL
ATTORNEY-CLIENT COMMUNICATION

May 1, 2012

Detroit City Council
1340 Coleman A. Young
Municipal Center
Detroit, Michigan 48226

Re: Legal Analysis of the Proposed Financial Stability Agreement Dated March 29, 2012— Validity Under the Default Limitation of the Michigan Home Rule City Act

Honorable City Council:

On April 1, 2012, in response to your request, I provided to Your Honorable Body a legal analysis of the proposed Financial Stability Agreement dated March 29, 2012, which had at that time been submitted to the Detroit City Council. A copy of this communication is attached hereto for your reference as Exhibit A. On April 4, 2012, the City Council adopted a resolution, a copy of which is attached hereto as Exhibit B, agreeing to the terms of the Financial Stability Agreement and directing and authorizing that the Agreement be signed on behalf of the City. Subsequently, Your Honorable Body through Council Member JoAnn Watson, has requested a legal opinion regarding whether pursuant to Section 7.5-205, Advice and Opinions of the Charter, "the Consent Agreement between the State of Michigan and the City of Detroit is valid." We are now responding to that request and providing the requisite information.

I

Is the City's Participation in the Financial Stability Agreement ("FSA") Barred by the Home Rule City Act?

The City of Detroit is organized and exists pursuant to the terms of MCL 117.1 *et seq.*, commonly known as the Michigan Home Rule City Act (the "Act"). This Act provides for the organization of cities, the formation and approval of their charters and states those powers which may and may not be provided for in municipal charters. Under Section 5(1)(f) of the Act, MCL 117.5(1)(f),a City is prohibited from entering into contractual arrangements with any person or entity that is "in default" to the City.[1] As the word "one" includes all persons or legal entities, it is very

[1] Section 117.5 states:

(1) A city does not have power to do any of the following:

...

(f) To make a contract with, or give an official position to, one who is in default to the city.

clear that the City would be prohibited from entering into a contract with the State of Michigan if it were determined that the State, at the time such a contract was entered into, was "in default to the City."

This provision of the Home Rule City Act was included in Section 2-113 of the 2012 Detroit City Charter, which states "(T)he City of Detroit through its Executive Branch departments and Legislative Branch agencies is prohibited from making a contract with, or giving an official position to, one who is in default to the City."

Section 13(1)(c) of Public Act 4 of 2011, the *Local Government and School District Fiscal Accountability Act*, commonly known as the "Emergency Manager Act," MCL 141.1501 through MCL 141.1531, authorizes a review team appointed under this Act to "negotiate and sign a consent agreement with the chief administrative officer of the local government." The Emergency Manager Act does not mention or refer to MCL 117.5(1)(f), or provide that the Home Rule City Act prohibition against a city contracting with one in default to the city does not apply to a consent agreement entered into under the Emergency Manager Act. In other words, since the Michigan Legislature did *not* provide in the Emergency Manager Act that "a Consent Agreement entered into under the Emergency Manager Act is not subject to MCL 117.5(1)(f) of the Home Rule City Act"(which prohibits a city from contracting with one "who is in default to the city"), then consent agreements cannot be entered into if a party to the agreement is in default to the contracting city.

II

Is the State of Michigan in Default to the City?

The Law Department is aware of three areas where the State of Michigan is in default to the City. These include:

1) **The outstanding bill for water and sewerage service at the State Fairgrounds amounting to $4.75 million.** (A summary of this claim is attached as Exhibit C).

2) **The failure of the State to fulfill its obligations regarding statutory revenue sharing resulting from the Agreement entered into between the City and the State in 1998.** (Documentation related to the State's default in regard to this matter is attached as Exhibit D).

3) **Accumulated unremitted claims against the State.** Nearly six hundred accumulated City of Detroit claims are pending against the State totaling approximately $300,000 in value. (A summary of these claims and the partial disposition thereof is attached as Exhibit E).

Item #1 above concerns bills that the City has submitted to the State over an extended period beginning in 2007 for water used at the State Fairgrounds. The State has disputed its liability for the amounts billed and failed to pay and remains in default to the City.

Item #2 above concerns the failure of the State to live up to the agreement that was reached between the City and the State in 1998 to reduce the City's income tax from three percent (3%) to two percent (2%) per cent and maintain revenues by holding annual statutory revenue sharing steady in the amount of $333,900,000.00 through the 2005-2006 Fiscal Year. This office has previously reviewed the effect of the State's failure to abide by this agreement and has reached the conclusion that the City did not have an enforceable claim for the funds lost. (See Law Department Opinion dated August 17, 2006 attached as Exhibit D-1 which summarizes the background and effect of this transaction). The fact that the City's loss is not recoverable, however, does not mean that the State is not in default to the City as that term is used in the Home Rule City Act. This is made clear in the opinion of Michigan Attorney General Mike Cox analyzing the meaning of this very term issued on February 10, 2010. (Attached as Exhibit D-2).

In his analysis, the Attorney General states: "Consistent with ... the plain and ordinary meaning of the word as used in MCL 117.5(1)(f) 'default' means the failure to fulfill a duty, whether arising from contract or otherwise, that a person owes to the City." He goes on to say that "(I)n addition, the statutory language selected by the legislature – "in default" – makes plain that an "alleged" default or a "challenged" default would not qualify."

The fact that the State does not challenge that it is in default on the 1998 agreement has recently been made clear by statements made by the State Treasurer Andy Dillon. In remarks delivered on the Inside Detroit radio show on WCHB-AM and reported on January 3, 2012, Mr. Dillon stated:

> "The state failed to live up to that 10 year deal and if you add up the last revenue sharing it totals up to $224 million. So, we don't deny that deal was not kept... ." (See article from the Click on Detroit website attached as Exhibit D-3).

Where it is undisputed that the State is in "failed to live up" to its agreement with regard to a well-publicized commitment, and for a major sum, we do not believe that it can be doubted that the State is in default to the City within the meaning of MCL 117.5(1)(f).

With regard to Item #3 above, we note the letter dated April 20, 2012 from the Michigan Department of Treasury. This letter states that not all claims for unclaimed property being held by the State have been paid, although the State fails to designate which claims will be paid and which will not. As to those claims that the State has refused to pay, it is clear that a default exists.

III

The 2012 Charter Requires the Corporation Counsel to Advise Public Officials of Charter Violations

The 2012 Detroit City Charter now contains a provision which requires the Corporation Counsel to enforce the Charter. Section 7.5-209 of the 2012 Charter provides:

Sec. 7.5-209. Enforcement of Charter.

The Corporation Counsel shall be responsible for enforcing compliance with the Charter. Corporation Counsel shall document in writing any violation of the Charter by the executive or legislative branches, Office of City Clerk, elected official or other persons subject to compliance with the Charter. This written notice shall contain the nature of the violation, including the Charter section(s) violated, direct the necessary action to be taken to remedy the violation, and date by which the remedial action must be taken. The time for taking the required remedial action shall not exceed fourteen (14) calendar days. The notice of Charter violation shall be presented to the offending body or individual, with a copy provided to the Mayor, City Council and City Clerk.

In the event the offending body or individual fails to remedy the Charter violation within the time frame and manner required in the written notice, Corporation Counsel shall take all reasonable actions to secure compliance, including, but not limited to, judicial action.

Nothing in this section is meant to waive any right to attorney-client privilege.

Given this new Charter-mandate, it is the obligation of the Corporation Counsel to advise this Honorable Body of the fact that the Consent Agreement entered into between the City of Detroit and the State of Michigan may violate Section 2-113 of the 2012 Detroit City Charter.

Conclusion

With respect to all the claims reviewed above, it is arguable as to whether the State is in default to the City within the meaning of Section 5(1)(f) of the Home Rule City Act, MCL 117.5(1)f).. For this reason, it is questionable whether there can be a contractual relationship between the City and the State, and whether there could have been at the time the Financial Stability Agreement was purportedly entered into between the parties.

I thank you for your attention to this matter. If you have any further questions, please feel free to contact me.

Respectfully submitted,

Krystal A. Crittendon

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Corporation Counsel