



Recovery Process for Two Financially Distressed Cities

Washington DC Financial Control Board and the City of Detroit Financial Emergency



Congress Asked GAO To Review Causes of Financial Crisis In DC

- Review and testimony focused on several areas
 - What gave rise to DC's financial crisis?
 - Why wasn't the crisis detected and reported by DC's external auditor?
 - How did other financially troubled cities address their financial crisis?
 - New York
 - Philadelphia
 - Cleveland
 - How should the Congress respond to City's financial crisis?



District of Columbia

What Caused the Financial Crisis

- Declining population and revenue – no strategies to adjust budget
- Government was bloated
- Disconnect between available cash and budget authority
 - DC General Hospital loans were really subsidies
 - Changing property tax year – created budget revenue but no cash to fund expenditures
 - Poor collection of taxes – No one took tax enforcement seriously
 - Looming unfunded pension liability
- Services deteriorating
- Lengthy and ineffective procurement process



Creation of Control Board Act

- Created a Board of 5 people appointed by the President of the U.S.
 - All the powers of previous control boards from other cities and the power to pass or reject laws of the District of Columbia Council
 - Power to declare any position no longer needed
 - Power to create a staff of professionals led by an Executive Director
- Created a CFO appointed by Mayor with advice and consent of Control Board
 - Once appointed, could only be removed by Control Board
 - All financial staff of City reported to and served at pleasure of CFO
 - Independent from Mayor, and has the last word on revenue estimation, financial impact of legislation, and whether budget was balanced. Position continues to this day

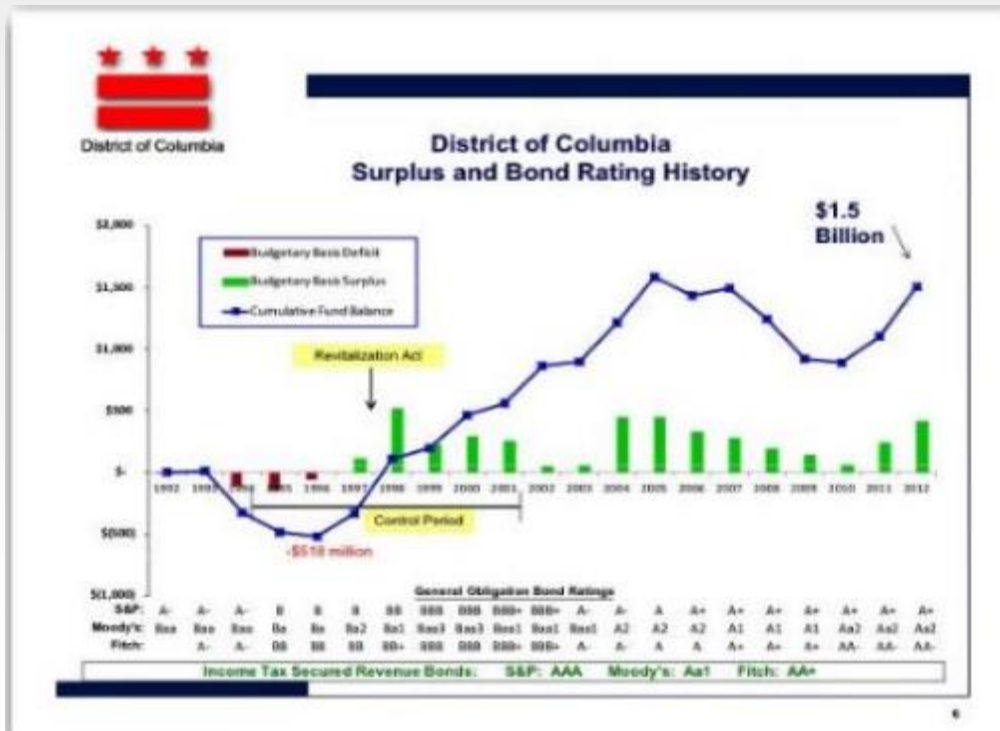


Creation of Control Board Act (cont.)

- Set criteria to meet in order for Control Board to sunset
 - 4 years of balanced budget
 - 4 years of unqualified audit opinions
 - Repayment of all borrowings from Treasury
 - Ability to meet all obligations in the normal course of business
- Control Board sunset was about 6 years after its creation
- Control Board will be called up again if any of the issues mentioned in the criteria reoccur
- Independent CFO remains with all financial staff at will and independent authority to set revenue projection



Financial Results of Control Period





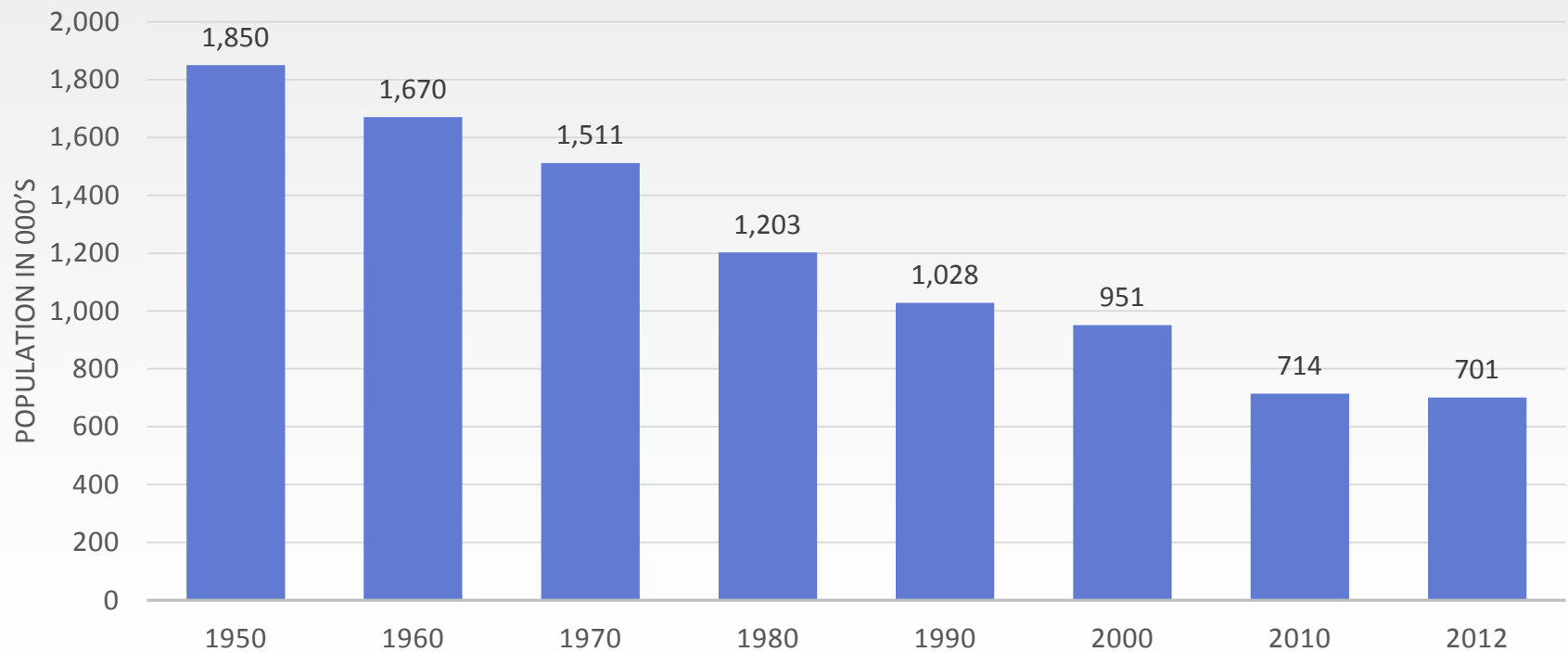
City of Detroit

What Caused the Financial Crisis

- Loss of jobs and steady decline in number of residents over many years
- Significant depletion of cash- projections estimated a cumulative cash deficit of \$100M by June 30, 2013
- General fund had not experienced a positive fund balance since FY2004. Without debt issuances, accumulated deficit would have been \$937M
- As of June 30, 2012, the City's long term liabilities, including unfunded actuarial accrued pension liabilities and OPEB, exceeded \$14B
- Disinvestment in infrastructure and systems of control

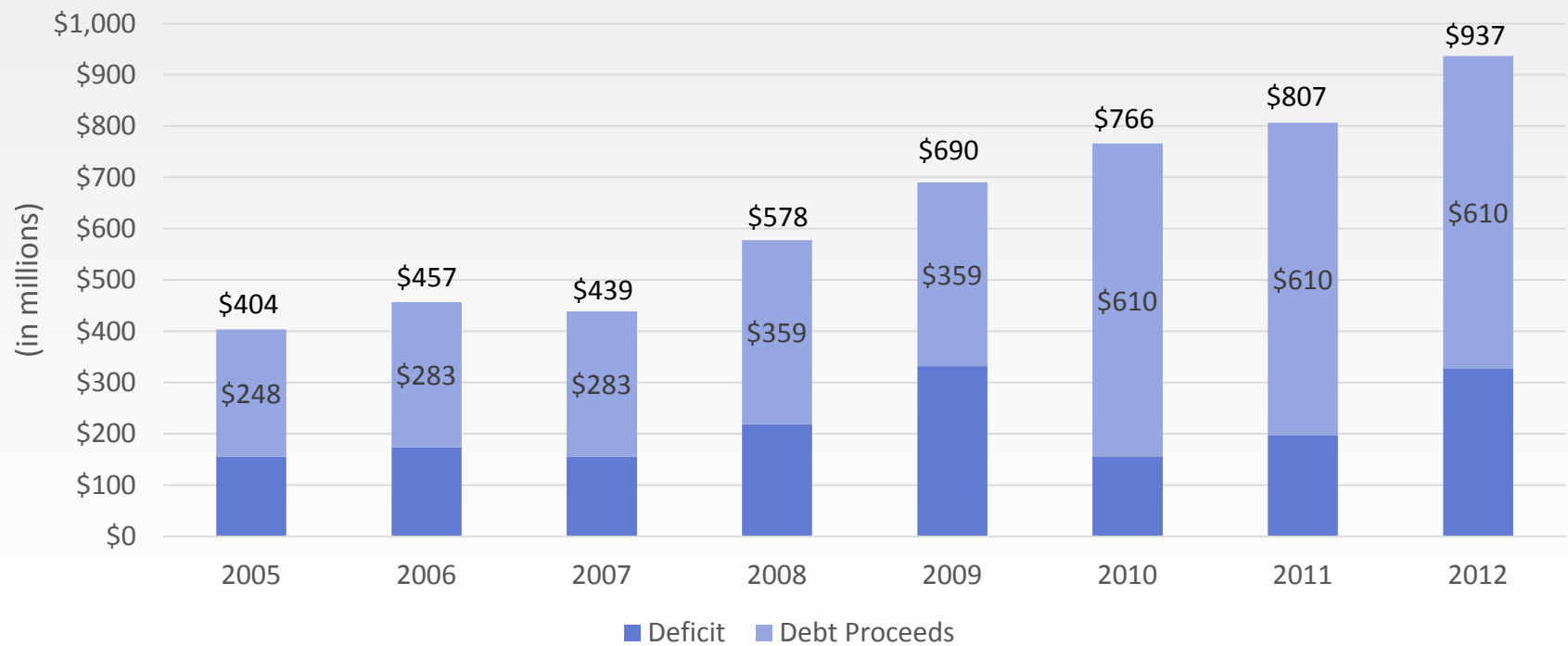


Population Decline of Over 60%





General Fund Accumulated Deficit





History of Financial Emergency

- December, 2012- Preliminary review leads State of MI's Treasurer, Andy Dillon, to conclude a serious problem exists and recommends the appointment of a Financial Review Team
- February, 2013- Financial Review Team unanimously concluded that no satisfactory plan exists to resolve the City's financial problems
- March, 2013- Governor Snyder declared a financial emergency and appointed Kevyn Orr as Emergency Manager



History of Financial Emergency (cont.)

- May, 2013- Preliminary financial and operating plan submitted to State Treasurer, stating Detroit's cash flow crisis made it insolvent and unable to borrow
- June, 2013- Published creditor plan, including pension and retiree health care cuts, offers of less than 10 cents on the dollar to some creditors, decision to stop unsecured debt payments
- July, 2013- Filed petition for municipal bankruptcy in U.S. District Court
- December, 2013- Judge Rhodes ruled Detroit was eligible for bankruptcy, insolvent, and dismissed challenges to the State's Emergency Manager law and ruled that pensions are not protected by the State Constitution



Financial Recovery is Underway

- Plan of Adjustment filed with the Court
- Court ordered mediation with major creditors are occurring
- \$120M of Post Petition Financing for restructuring efforts, with a focus on capital spending and blight remediation, has been approved by Court
- Detroit hopes to exit bankruptcy by October 15, 2014



Must Be A Greater Strategy Around Recovery

- Goals must be clearly defined and achievable
- Must explain to the citizens what is happening and why
 - Analysis of problems and solutions tap into service improvements, our citizens deserve better
 - Fix internal systems and publicize efforts that citizens will understand
 - Tax returns – high profile cheats
 - Records in disarray – quick refunds
 - Trash pick up, education, procurement process, community policing
- Must engage elected officials in reform



City of Detroit: A Complicated Recovery

- A new Mayor and a restructured council- must develop a strategy for meaningful engagement or unconstructive power plays are inevitable
- Many of the major systems that reforms depend on are broken- **Must Stabilize Systems**
- Short time period, conditions that give rise to sunset of Emergency Manager may not be met- Is there a need for independent CFO function for period of time?
- Multiple recovery plans by various stakeholders, no clear implementation
- Post Bankruptcy structure still under review with various models being suggested
- Role of Detroit's business community in reform to be determined- DC business community played a major role in supporting key reforms in the District of Columbia



Plan of Adjustment to Drive Recovery

- Invest approximately \$1.5 billion over 10 years to, among other things:
 - Improve and provide essential municipal services to the City's 700,000 residents, including police, fire and emergency medical services, garbage removal and functioning streetlights
 - Attract and retain residents and business to foster growth and redevelopment
 - Improve the City's information technology systems, thereby increasing efficiency and decreasing costs
- Provide pension treatment that is intended to deliver pensions that the City can afford and by which retirees can continue to meet their needs
- Lay the foundation for a solvent Detroit that can live within its means and meet realistic obligations
- Continue to explore various management and ownership options for water and sewer department
- Emphasize negotiated solutions- including through continued federal mediation- that maximize creditor recoveries while allowing the City to meet its obligations and have a viable future



Key Differences: DC Compared to Detroit

- Congress acted quickly to provide direct oversight of DC government
- Delays in addressing financial crisis in Detroit have made it much more difficult to address
- DC was 6 years under control period
- Detroit post bankruptcy structure and length of time is yet to be determined