



Democracy for Sale: Subverting Voting Rights, Collective Bargaining and Accountability under Michigan's Emergency Manager Law

Interim Report and Recommendations of the
House Judiciary Committee Democratic Staff

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Table of Contents

Background Facts	1
Findings	3
I. The EM Is Unconstitutional Because It Violates the Contracts Clause of the Constitution	3
A. What Public Act 4 Provides	3
B. What the Constitution Provides	4
C. How the EM Law Violates the Contract Clause	4
1. The EM Law Authorizes the Substantial Impairment of Collective Bargaining Agreements	4
2. Public Act 4 Does Not Promote a Legitimate Public Purpose	5
3. Public Act 4 Fails the Reasonable and Necessary Requirement for Constitutional Sufficiency	6
D. A Constitutional Alternative to the EM Law Already Exists	7
II. Other Controversial Aspects of the EM Law Will Likely Lead to a Legal Morass	8
A. Limiting Voting Rights and Representative Government	8
B. Possible Violation of Other Michigan and State Constitutional Protections	11
C. Violations of Michigan's Open Meetings Act	12
D. Possible Invalidity of Stop-Gap Measures to Thwart Citizen's Petition Drive	13
III. The Michigan EM Law Has Not Worked	13
A. Inconsistent Application and Failure to Meaningfully Strengthen Jurisdiction's Finances	13
B. Examples of Abuse, Mismanagement, and Conflict of Interest under the Michigan EM Law	14
Recommendations	16
I. New Legislation is Needed	16
II. A Multi-Pronged Approach is Needed to Respond to the Economic Harm Cause by the Loss of Manufacturing Jobs and the Recession	17
A. Role of Local Government	17
B. Role of State Government	17
C. Role of the Federal Government	18
III. Greater Oversight of the EM Law is Needed	19
End Notes	21
Appendix	26
Michigan Emergency Manager Chronology	

Michigan Emergency Manager Law, Final Enrolled Bill

Emergency Manager Law Description

Internal Bill Analysis of Emergency Manager Law, Prepared by Michigan Department of Treasury

Letter to Department of Justice from Ranking Member Conyers, December 1, 2011

Forum Witness Testimony

Statement on Constitutionality of Michigan Emergency Law Prepared by
Professor Kenneth N. Klee, UCLA School of Law

Statement on Compliance with Voting Rights Act of Michigan Emergency
Manager Law Prepared by Professor Jocelyn Benson, Wayne State Law School

Statement of Joseph L. Harris, Emergency Manager, City of Benton Harbor, MI

Statement of John C. Philo, Legal Director, Sugar Law Center

Statement of James Spiotto, Chapman and Cutler, LLP

Background Facts

Public Act 4, the Michigan Emergency Manager Law, has evolved considerably over time. It originated in 1986 when the Wayne County Circuit Court appointed Louis Schimmel as the financial receiver for the City of Ecorse, which was facing a \$6 million deficit. (Schimmel would go on to serve as the Emergency Financial Manager ("EFM") for Hamtramck and is the current Emergency Manager ("EM") for Pontiac.) In 1988, in response to the Ecorse court decision, the state legislature passed PA 101, statutory EFM legislation, which was signed by Governor Blanchard. This statute authorized the state to intervene in the affairs of local governments facing a "financial emergency." The law was used in connection with financial problems in River Rouge and Royal Oak.

Two years later in 1990, Governor Blanchard signed a new, broader EFM law, PA 72, setting forth a more formal financial review process. PA 72 also provided for the possibility of consent agreements whereby local officials negotiated with the state to develop a plan to resolve financial emergencies. PA 72 did not permit unilateral cancellation of collective bargaining agreements or grant academic control to EFM's appointed to operate school districts. The law was used to appoint EFM's in Hamtramck (2000-2007); Highland Park (2001-2009); Flint (2002-2004); Inkster Public Schools (2002-2005); Village of Three Oaks (2008-2011); Detroit Public Schools (2009-present); Pontiac (2009-present); Ecorse (2009-present); Benton Harbor (2010- present); and to reach a consent agreement with River Rouge (2009).

In March 2011, the new Republican Majority in Lansing under newly elected Republican Governor Snyder enacted a far broader and more draconian EM law, PA 4. Among other things, the new law gives an EM the power to completely take over governance of an impacted jurisdiction, becoming a one-person mayor, city manager and city council (or school board and superintendant); abrogate existing collective bargaining contracts; and make academic decisions in place of elected school boards (overturning an earlier court decision involving the Detroit Public Schools) (see the Appendix for a more comprehensive description of the current EM law). The new EM law had the effect of immediately broadening the authority of the current EM's operating the Detroit Public Schools, Pontiac, Ecorse, and Benton Harbor, and was used to appoint new EMs in Flint (for the second time) and the Highland Park Public Schools. In addition, under the EM law, financial reviews have been initiated for Inkster, the City of Detroit, and the Muskegon Heights Schools.

A significant part of the impetus for the new broadened law appears to be motivated by a desire to target public employees' collective bargaining rights. In states such as Ohio and Wisconsin, this motivation took the form of legislation which eliminated these rights directly. The Michigan law, by contrast, did so through Emergency Managers. A February 15 article in Mother Jones highlights the connection between the Michigan EM Law and the conservative

Mackinac Center for Public Policy—a free-market think tank funded, in part, by foundations of conservative billionaire Charles Koch, the Walton family, and Dick DeVos. The Mackinac Center is a member of the American Legislative Exchange Council (“ALEC”) —a clearinghouse for privatization efforts and legislation linked to various states anti-immigration law and voter ID laws, and Wisconsin and Ohio’s bans on municipal employees’ collective bargaining rights. The article notes that Louis Schimmel, an ardent advocate of “privatization” of public services, is a former adjunct scholar and director of municipal finance at the Mackinac Center; that in 2005 Mackinac published an essay by Schimmel calling on Michigan’s legislature to grant emergency managers the power to negate collective bargaining agreements and eliminate elected officials; that the Mackinac Center has touted the savings the State of Michigan could realize if it reduced public employee benefits; and that ALEC has been supporting laws like Michigan’s EM law as a way to target public employees and identify privatization opportunities.¹

The new EM Law has proven to be extremely controversial. As a result, a series of lawsuits have been brought challenging the new law: the Detroit Pensions Boards filed a lawsuit alleging constitutional violations (which was dismissed on “ripeness” grounds); numerous Michigan residents filed suit alleging state constitutional violations (which remains pending); and Highland Park School Board Member Robert Davis successfully sued the State on the ground that certain financial review board meetings violated the Michigan Open Meetings Act (thereby nullifying the appointment of the EM for Highland Park Public Schools, as well as the process being used to consider an appointment in the City of Detroit).

The adoption and implementation of the law also led to the following:

- Rep. John Conyers, Ranking Member on the House Judiciary Committee, has called for a federal legal review by the Department of Justice.
- Scores of federal and state legislators and various non-profit organizations have written to ask for intervention by state and federal officials.
- Numerous protests, public forums and growing local and national media attention, including coverage by the “Rachel Maddow Show,” “Ed Shultz Show,” “Al Sharpton Show,” The New York Times, the Nation, and Mother Jones.
- An organized petition drive by Michigan Forward to place an initiative on the November ballot to overturn the EM law, which would “freeze” the law until the election (which in turn has led the Michigan legislature to consider enacting a so-called “stop gap” law to thwart the petition drive).

Findings

I. The EM Law Is Unconstitutional Because It Violates the Contracts Clause of the Constitution

By unilaterally authorizing the EM to terminate collective bargaining agreements, the law clearly violates the U.S. Constitution's Contracts Clause, which generally prohibits a state from impairing contracts.

The EM Law presents significant and substantial constitutional concerns particularly with respect to the powers it gives to the EM to impair collective bargaining contractual obligations in violation and other contracts in violation of the Contracts Clause of the U.S. Constitution. As Kenneth Klee, the Nation's preeminent constitutional bankruptcy scholar, and a former Republican staffer on the House Judiciary Committee, concludes in his attached written statement concerning the EM Law, "as currently drafted, the [Michigan EM Law] is violative of the Contracts Clause ... No prior legislature has had the audacity to legislate the unilateral termination, rejection, or modification of a collective bargaining agreement."²

A. What Public Act 4 Provides

In pertinent part, Public Act 4 permits the EM – in his or her "sole discretion" – to reject, modify or terminate a collective bargaining agreement, after conferring with the appropriate bargaining representative.³ The law authorizes such action as a "legitimate exercise of the state's sovereign powers if the emergency manager and state treasurer determine" that certain specified conditions are satisfied.⁴ In addition, the EM may reject, modify, or terminate an existing contract.⁵

The criteria set forth in Public Act 4 for rejecting, modifying or terminating a collective bargaining agreement are as follows:

(i) The financial emergency in the local government has created a circumstance in which it is reasonable and necessary for the state to intercede to serve a significant and legitimate public purpose.

(ii) Any plan involving the rejection, modification, or termination of 1 or more terms and conditions of an existing collective bargaining agreement is reasonable and necessary to deal with a broad, generalized economic problem.

(iii) Any plan involving the rejection, modification, or termination of 1 or more terms and conditions of an existing collective bargaining agreement is directly related to and designed to address the financial emergency for the benefit of the public as a whole.

(iv) Any plan involving the rejection, modification, or termination of 1 or more terms and conditions of an existing collective bargaining agreement is temporary and does not target specific classes of employees.⁶

B. What the Constitution Provides

Collective bargaining agreements are contracts. As such, they are covered by the Contracts Clause of the U.S. Constitution, which provides that “[n]o State shall . . . pass any . . . Law impairing the Obligation of Contracts[.]”⁷ The provision applies to contracts entered into between private parties as well as public contracts. As the U.S. Supreme Court explained, the Contracts Clause “limits the power of the States to modify their own contracts as well as to regulate those between private parties.”⁸ Impairment, within the meaning of the Contracts Clause, means a state law that renders the obligations of a contract “invalid, or releases or extinguishes them[.]”⁹

Notwithstanding the literal dictates of this provision, the Supreme Court has recognized certain exceptions where states may impair contracts in order “to safeguard the welfare of their citizens.”¹⁰ In the midst of the Great Depression, the Supreme Court promulgated a test to determine whether state impairment of a contract is constitutional in *Home Building & Loan Ass’n v. Blaisdell*.¹¹ Over the years, this test has evolved into three basic components: (1) is the contractual impairment substantial and, if so, (2) does the law serve a legitimate public purpose such as remedying a general social or economic problem and, if such purpose is demonstrated, (3) are the means chosen to accomplish this purpose reasonable and necessary.¹²

C. How the EM Law Violates the Contract Clause

1. The EM Law Authorizes the Substantial Impairment of Collective Bargaining Agreements.

Public Act 4 specifically authorizes the EM to “reject, modify, or terminate 1 or more terms and conditions of an existing collective bargaining agreement” on a temporary basis.¹³ The EM is given the authority to exercise this power in his or her “sole discretion.”¹⁴ Without question, Public Act 4 gives the EM “broad power . . . to severely impair the bargained-for rights of public employees in a broad, indiscriminate, and indefinite manner.”¹⁵

For example, the Supreme Court considered in *Home Building & Loan Assn. v. Blaisdell* whether a state law, enacted in the midst of the Great Depression, that temporarily impaired a mortgagee's contractual rights.¹⁶ The law extended the redemption period for home foreclosures, but required the homeowner to pay the mortgagee a reasonable rental value of the property during such period. The Supreme Court found that the state law did not violate the Contracts Clause *inter alia* because it did not constitute a substantial impairment. The Court reasoned:

The statute does not impair the integrity of the mortgage indebtedness. The obligation for interest remains. The statute does not affect the validity of the sale or the right of a mortgagee-purchaser to title in fee, or his right to obtain a deficiency judgment if the mortgagor fails to redeem within the prescribed period. Aside from the extension of time, the other conditions of redemption are unaltered. While the mortgagor remains in possession, he must pay the rental value as that value has been determined, upon notice and hearing, by the court. The rental value so paid is devoted to the carrying of the property by the application of the required payments to taxes, insurance, and interest on the mortgage indebtedness. While the mortgagee-purchaser is debarred from actual possession, he has, so far as rental value is concerned, the equivalent of possession during the extended period.¹⁷

A major distinction, however, can be made between the EM's authority under the EM Law and an instance where, for example, a state imposes a temporary moratorium on home foreclosures. Whereas the former impermissibly terminates contracts rights outright, the latter merely delays the right of a party to exercise its contractual rights. And, as the Supreme Court has observed, the "severity of the impairment measures the height of the hurdle the state legislation must clear."¹⁸ Public Act 4, by authorizing the termination of collective bargaining agreements, constitutes a severe impairment of the rights the private parties to these contracts and thus violates the Contracts Clause of the U.S. Constitution.

2. *Public Act 4 Does Not Promote a Legitimate Public Purpose*

The Supreme Court has held that state action constituting a severe impairment of contractual rights "will push the inquiry to a careful examination of the nature and purpose of the state legislation."¹⁹ Public Act 4 specifies certain determinations that must be satisfied before an EM may terminate a collective bargaining agreement. For example, the EM Law requires a finding that the "financial emergency in the local government has created a circumstance in which it is reasonable and necessary for the state to intercede to serve a significant and legitimate public purpose."²⁰ Thus facially, Public Act 4 purports to ground the EM's authority to act on existence of a "financial emergency" warranting state intercession to serve a legitimate "public purpose."

The existence of a financial emergency, however, does not in and of itself substantiate a power grab. As the Supreme Court eloquently explained:

Emergency does not create power. Emergency does not increase granted power or remove or diminish the restrictions imposed upon power granted or reserved. The Constitution was adopted in a period of grave emergency. Its grants of power to the Federal Government and its limitations of the power of the States were determined in the light of emergency, and they are not altered by emergency. What power was thus granted and what limitations were thus imposed are questions.²¹

Accordingly, the resolution of this issue would depend on the nature of the financial emergency sought to be addressed by the Act in light of the contractual impairment involved. As Professor Kenneth Klee explains in the Appendix to this Report, “not every budget shortfall can properly be considered a financial emergency capable of supporting otherwise unconstitutional legislation.”²²

In addition, there may be concerns about the bona fide causes of the financial distress being experienced by certain municipalities in Michigan. As elsewhere noted in this Report, there are serious concerns that the State of Michigan may itself be contributing to the financial distress of certain municipalities by withholding long-promised payments. Absent clear evidence of a legitimate public purpose, rather than a concocted financial emergency, the termination of collective bargaining rights under Public Act 4 would be unconstitutional.

3. *Public Act 4 Fails the Reasonable and Necessary Requirement for Constitutional Sufficiency*

Public Act 4 facially qualifies the EM’s power to terminate a collective bargaining agreement by limiting it to “a circumstance in which it is reasonable and necessary for the state to intercede.” At the same time, however, the Act empowers the EM to use his or her “sole discretion” in determining whether to reject, modify or terminate a collective bargaining agreement²³ and is completely silent as to whether the EM must first attempt any other remedies.

With respect the “reasonable and necessary” criterion, courts typically consider whether a more moderate alternative existed. For example, the Second Circuit, in considering a state law that imposed a two-week payroll lag on non-judicial employees of the state’s court system, found that this law unconstitutionally impaired a collective bargaining agreement because there were alternatives available to the state to alleviate the financial distress.²⁴

Arguably, the fact that any rejection, modification or termination of a collective bargaining agreement may only have a temporary duration²⁵ could be viewed as having a less draconian impact. Nevertheless, Public Act 4 fails to provide any guidelines as to what is meant by "temporary." Indeed, even a temporary termination of a municipality's contractual obligation to pay stated wages, protects jobs, or provides health insurance could be devastating.

D. A Constitutional Alternative to the EM Law Already Exists

Of particular concern is the fact that Public Act 4 virtually ignores a thoroughly constitutional alternative that would permit the rejection, modification, or termination of collective bargaining agreements. Chapter 9 of the Bankruptcy Code is a specialized form of bankruptcy relief²⁶ that permits a municipality²⁷ "to seek protection from its creditors while it formulates and negotiates a plan for adjustment of its debts, either extending maturities, reducing interest or principal, or refinancing its debt by obtaining a new loan elsewhere to pay off existing debt, in whole or in part, and to provide the mechanism by which the plan that is acceptable to the majority of creditors can be made binding on a recalcitrant and dissenting minority."²⁸

While the Constitution specifically prohibits a state from "impairing the Obligation of Contracts,"²⁹ the Constitution does authorize Congress to promulgate "uniform Laws on the subject of Bankruptcies throughout the United States."³⁰ Bankruptcy, therefore, provides a constitutional means to address contractual obligations.

With respect to collective bargaining agreements, Chapter 9 permits the assumption or rejection of executory contracts pursuant to Bankruptcy Code section 365.³¹ In interpreting the application of section 365 to a collective bargaining agreement, the Supreme Court has held that a court, before it may authorize the rejection of such agreement, must find that it is burdensome to the debtor and that rejection is favored, balancing the equities.³² Parties to the contract, such as the employees, would be entitled to appear in court and present evidence on the issue of burdensomeness.³³ In addition, Bankruptcy Code section 903 requires the municipality to comply with state law, which serves as the "constitutional mooring for chapter 9 as it embodies a statutory declaration that the enactment of municipal bankruptcy law pursuant to Article I, Section 8 of the United States Constitution does not limit or impair the rights reserved to the States pursuant to the tenth amendment."³⁴ As a result, a municipality's "right to make unilateral changes to a collective bargaining agreement is not unfettered."³⁵

Rather than facilitating the use of Chapter 9, however, the EM Law imposes a cumbersome process in addition to what the Bankruptcy Code already requires.³⁶ PA 4 permits a municipality to file for bankruptcy relief only after an EM is appointed and only if he or she recommends such relief and the governor approves it.³⁷ The recommendation to the governor and the state treasurer must include either of the following:

- (a) A determination by the emergency manager that no feasible financial plan can be adopted that can satisfactorily rectify the financial emergency of the local government in a timely manner.
- (b) A determination by the emergency manager that a plan, in effect for at least 180 days, cannot be implemented as written or as it might be amended in a manner that can satisfactorily rectify the financial emergency in a timely manner.³⁸

As a result, the EM Law forces a municipality to undergo the appointment of an EM before it can be considered for Chapter 9.³⁹

II. Other Controversial Aspects of the EM Law Will Likely Lead to a Legal Morass

Provisions impacting minority voting rights and representative form of government; provisions in possible violation of the state constitution; implementation in violation of the Michigan Open Meetings Act; and consideration of possible “stop-gap” legislative fixed designed to thwart the voter initiative process are all controversial and largely untested in the courts due to the extreme and unprecedented nature of the EM Law and could take years to resolve, potentially leading to financial disarray and gridlock.

As highlighted in the attached Michigan EM Chronology, the most recent iteration of the EM law has led to a plethora of lawsuits and legal controversies – some have been successful, some have been dismissed, at least temporarily, while others remain pending. Due to the unprecedented powers granted to the Michigan Treasurer and EMs under the legislation, many of the legal issues presented constitute cases of first impression. While it is difficult to predict with certainty the outcome of these legal disputes, it does appear likely the ongoing and persistent nature of the ensuing legal controversies will hinder rather than assist financially troubled local governments from obtaining the relief and certainty they and their residents need. The following is a summary of these legal disputes:

A. Limiting Voting Rights and Representative Form of Government

Section 2 of the Voting Rights Act prohibits voting practices or procedures that discriminate on the basis of race, color, or membership in a language minority group. There is little dispute that implementation of the EM Law has a significant impact on voting rights in local elections, and has had a disproportionate impact on minority voting rights in such elections. Consider the following:

- An internal analysis of PA 4 prepared by the Snyder Administration reveals that the bill’s very proponents are well aware of this concern. A Department of Treasury analysis

states, “[t]his bill allows emergency managers too much power and control over local units of government. Emergency managers can’t be trusted to act in the interests of the local unit and will use the enhanced powers granted under this bill for their own gain. Stripping local officials of the powers is anti-democratic.”

- The Benton Harbor EM, Joe Harris, has all but voided local elected government. Harris eliminated the power of the mayor and city commissioners (they are only permitted to call meetings to order, adjourn them and approve minutes) and fired the finance director and city manager.
- Such actions by necessity discourage voters from participating in elections. As *The New York Times* recently noted, ““one of the biggest challenges facing Benton Harbor is the city’s staggering level of political disengagement, which has made it almost impossible to know what residents want from their representatives. In the [most recent] citywide election only about 1,400 of Benton Harbor’s citizens voted; in 2009, the turnout was less than half that. Democracy has now officially been suspended in Benton Harbor.”⁴⁰
- If Detroit and Inkster are subject to EM’s, that would mean the percentage of African-Americans without representative local government under the EM law will be 50.7% of the African American residents of the state according to census data:

City	Population	% African American	# of African Americans
Benton Harbor	10,038	89.2%	8,954
Detroit	713,777	82.7%	590,294
Ecorse	9,512	46.4%	4,414
Flint	102,434	56.6%	57,978
Inkster	25,369	73.2%	18,570
Pontiac	59,515	52.1%	31,007
Total			711,217

Although the specific facts presented by the implementation of Michigan's EM Law are untested in court, the legal implications of denying local votes to more than 50% of African American voters in a large state raises serious and important legal questions. This specific question was reviewed by voting law and rights expert, Professor Jocelyn Benson, of Wayne State University, who submitted the attached statement as part of the February 21 Forum. Professor Benson notes that Section 2 claims require a court to evaluate the "totality of the circumstances" of the law's enforcement. "In other words, the court must examine the overall context of the election systems to determine whether the challenged election law causes minority voters to have 'less opportunity than other members of the electorate to participate in the political process and to elect representatives of their choice'."⁴¹ While Professor Benson notes the EM Law itself is facially neutral, she concludes that "there is significant evidence [the] amended Emergency Financial Manager law has a disproportionate impact on the state's Black and Latino population." She reaches this conclusion for the following reasons:

- If Detroit and Inkster become subject to EM's, as the above chart notes, this would mean that more than half of the African-American voters are disenfranchised in local elections. "This would suggest that, under the totality of the circumstances, this law's application and enforcement would result in African Americans having less opportunity for self-governance than other members of Michigan's electorate."
- Enforcement of the EM Law "does send an implicit message of disempowerment and suppression. Imagine going to the polls on Election Day to vote in your city election, only to hear on the radio that your vote for mayor will likely be overruled by a state authority appointing an emergency manager to take over the city? That is exactly what happened in Flint – a majority Black city - last November, when state officials announced on Election Day that they would likely appoint an emergency manager to oversee Flint's finances after declaring a financial emergency in the city."
- There are other, less intrusive means of protecting the state's interest in having financially solvent jurisdictions, without such a broad based limitation on local voting rights. "At the very least, in times of financial emergency, managers should be appointed with the consent of the citizens over which they will have authority. And those citizens should not only have a say in who is appointed as manager, they should also be able to have the ability to remove a manager who has abused their power or exceeded their authority without the current high hurdles in the law [In addition] The managers should ... be permitted to only implement temporary changes, and make a recommendation for any long term or permanent changes that can best address the crisis. Citizens should then be given the opportunity at the next possible election date to review

and vote on enacting aspects of those recommended changes - thereby empowering voters to direct their state and city on the solutions they would like to see implemented.”

The Michigan EM Law also raises broader questions about the states commitment to the principal of a republican form of government as envisioned under both the State and U.S. Constitution. PA 4 has the potential to frustrate representative democracy as envisioned by Art I §1 of the Michigan Constitution, which provides that “all political power is inherent in the people. Government is instituted for their equal benefit, security and protection.” Further, the U.S. Constitution guarantees all States a republican form of government under Art 4 §4, which courts have held is one that is democratically elected.⁴² Again, while the specific facts are untested legally due to the extreme nature of the Michigan law, there is some legal precedent which indicates that the EM Law may run afoul of the general legal principals set forth in the Michigan and U.S. Constitutions:

- The Michigan Supreme Court in *Dearborn Fire Fighters Union v. Dearborn* recognized that rooted in Art I §1 is a “core concept of representative democracy:” “the political power which the people possess and confer on their elected representatives is to be exercised by persons responsible (not independent) and accountable to the people through the normal processes of the representative democracy.”⁴³
- The Dearborn court acknowledged that independent outsiders may resolve an “immediate crisis,” the delegation of public responsibilities to private parties effectively eliminates the ability of the public to monitor and observe the public performance of such private actors, and to hold such actors accountable for any unacceptable conduct.⁴⁴ This is problematic because the EM in Michigan is not required to consult with any of the local governing bodies, nor is there a system in place which allows the public to scrutinize and/or remove an ineffective or abusive emergency manager.

B. Possible Violation of Other Michigan and State Constitutional Protections

The Michigan EM Law also raises several complex and largely untested questions under Michigan’s Constitution – whether the law violates the constitution’s “non-delegation doctrine”; whether it violates the “local acts” clause specifically and separation of powers principals generally; whether it violates the “elector’s right to form charter” clause; and whether it violates the unfunded mandate requirement. Consider the following:

- Michigan’s non-delegation doctrine⁴⁵ may be violated by provisions in the EM Law providing for consent agreements that, without a finding of a financial emergency and without reasonably precise limiting standards, permit the state treasurer to delegate sole

discretionary legislative power to a local government's chief administrative officer, the chief financial officer, or other executive officers of the local government.

- Michigan's local acts clause⁴⁶ and separation of powers principles may be violated by the EM Law delegating more power than the legislature possesses. Specifically, PA 4 may violate the clause by granting emergency managers sole discretionary power and authority to contravene, and thereby repeal, amend and enact local laws such as city and village charters and ordinances.
- Michigan's elector's right to form charter clause,⁴⁷ which vests city and village electors with exclusive power to "frame, adopt and amend its charter;" may be violated by the EM Law granting the State Treasurer sole discretion to appoint an emergency manager with powers suspend, repeal, or amend city and village charters violates this provision.
- Michigan's unfunded mandate protection may be violated by the EM law requiring the use of local taxpayer dollars for such purpose and managers' salary and staff and paying legal expenses associated with the law.

C. Violations of Michigan's Open Meetings Act

Implementation of the EM Law has recently been found by a court to violate one specific provision of Michigan law – the Open Meetings Act. Michigan Public Act 267, better known as the "Open Meetings Act of 1976," was created to strengthen the transparency of government business, and requires public institutions to conduct nearly all business at open meetings. The Act requires government bodies to provide notice to the public and keep meeting minutes. Should a government hold a private meeting in violation of the Act, decisions conducted within that meeting is invalidated, and actions stemming from such meetings can be repealed.⁴⁸

On February 2, 2012, Ingham County Circuit Court Chief Judge William Collete issued a bench ruling that Michigan's emergency manager financial review board must open their meetings to the public, in response to a legal challenge filed by Highland Park School board member Robert Davis against Treasurer Andy Dillon and Gov. Rick Snyder. Davis alleged that the closed-door process of the state-appointed Detroit financial review team violated Michigan's Open Meetings Act of 1976. A lawyer representing the State of Michigan publicly stated that they intend to appeal the Court's injunction to suspend the Detroit review team's meetings. That same week, Davis also filed suit against the appointment of Highland Park Schools EM, Jack Martin under the same claim. On February 15, 2012, Judge Collete again ruled that the State of Michigan violated the Open Meetings Act, and that the Highland Park review team's decisions are repealed. Consequently, Jack Martin's appointment as Highland Park Schools EM was nullified.⁴⁹

D. Possible Invalidity of Stop- Gap Measures to Thwart Citizen's Petition Drive

On December 15, 2011 the Michigan Senate passed a so-called "stop-gap" emergency manager bill, S.B. 865. This legislation was designed to allow emergency managers to remain in place even if a petition drive to freeze Michigan's emergency manager is successful. If the legislation (or a modified version) is brought up in the State House it will require a 2/3 vote to take effect immediately, otherwise its effective date must be delayed 90 days. It is unclear whether any final "stop-gap" law will rely on the older law PA 72, will allow new Emergency Managers to be appointed, or will even be legally valid.

III. The Michigan EM Law Has Not Worked

Experience under the Michigan EM Law indicates that it has not been used consistently and over the long term to meaningfully strengthen the finances of local jurisdictions; and there have been a significant number of cases of abuse, mismanagement, and conflict of interest.

A. Inconsistent Application and Failure to Meaningfully Strengthen Jurisdiction's Finances

As part of our review, we have identified numerous instances where the EM Law has not served to enhance or strengthen the finances of local jurisdictions which have been subject to its provisions:

- Ecorse – In 1986, financial difficulties in Ecorse led to the creation of the EM when a receiver was appointed to oversee the city's finances. Despite operating the Wayne County jurisdiction's finances for four years, a second EM was appointed in 2009 and remains in control of the city today. This means that overall; Ecorse has been under the control of an unelected official for seven years and counting.
- Hamtramck – Hamtramck was placed under control of an EM for seven years, from 2000-2007. Notwithstanding this control, the city remains in financial distress and has been unable to make pension payments. The state has been unwilling to approve Hamtramck's request to allow it to file for municipal bankruptcy.
- Highland Park – Highland Park was under EM control for eight years, from 2001-2009. The effectiveness of Highland Park's EFM has been questioned as it is back in the red. In August 2011, DTE, the electricity supplier for Highland Park, took out 1,400

streetlights because the city owed \$4.5 million on its power bill. The city is currently dealing with a \$1.5 million deficit.⁵⁰

- Flint – Flint has had two EM's appointed. It was first under the control of an EM from 2002-2006, and new EM was appointed in 2011 who remains in control today. The city's most recent audit showed the city ended the 2011 year with a \$7.3 million deficit, but would have been even deeper in the hole if the city had not borrowed \$8 million last year.
- Inkster – Both Inkster and its public schools have been reviewed under the EM Law. The School district was under EM control from 2002-2005 and a state review board is currently considering whether to appoint another EM to this city in Wayne County. Inkster was recently forced to lay off 20% of its police officers.
- Pontiac – Pontiac has been under the control of an EM for three years, beginning in March 2009. The EM does not appear to have enhanced the city's finances, as its credit rating has reportedly dropped from B to triple-C under the EM.
- Benton Harbor – Benton Harbor has been under the control of an EM for two years. Notwithstanding the consolidation of power under Joe Harris, it appears the city's financial problems remain ongoing. In the most recent fiscal year, an independent audit found that Benton Harbor (a) overspent its receipts by more than \$650,000; (b) suffered from material weaknesses in its controls over financial reporting; and (c) has not made required contributions to its employees' pension fund.⁵¹

As *The New York Times* has noted, questions have arisen as to why certain jurisdictions have been subject to EM's even though, "there are plenty of nearly broke towns in Michigan."⁵²

B. Examples of Abuse, Mismanagement, and Conflict of Interest under the Michigan EM Law

Our review has identified numerous examples of abuse, mismanagement and conflict of interest under the EM Law. Concerns have long been expressed that the EM Law would be used as a vehicle allowing for the privatization of public services. In this regard, the Mackinac Center for Public Policy, along with the American Legislative Exchange Council "has been supporting laws like Michigan's EM Law as a way to ... identify privatization opportunities."⁵³ These concerns appear to have been realized, as *New York Times* author Jonathan Maller has written, "I have seen the training materials for the training sessions held for potential E.M.'s, and they contain nothing that would help an E.M. develop academic and educational plans. In fact, the trainings were run primarily by representatives from companies who stand to benefit financially as E.M.'s outsource many of the tasks normally handled by a municipality or school district. This

is a big red flag for those of us who worry that PA 4 is a not-so-subtle vehicle for forcing privatization of our governments and schools.” By way of specific example, Chris Savage’s February 15, 2012 Nation article noted, “In Pontiac EFM Michael Stampfler outsourced the city’s wastewater treatment to United Water just months after the Justice Department announced a twenty-six-count indictment against the company for violating the Clean Water Act.”

Other specific examples of mismanagement and abuse that have been identified include the following:

- Highland Park -- Emergency Manager Arthur Blackwell II was terminated in 2005 for taking \$264,000 in payments not authorized by State even though he had publicly announced he would serve for an annual salary of one dollar. In 2011, Blackwell was ordered to repay these amounts.
- Pontiac -- In addition to the outsourcing of water treatment work to a company charged with violating the Clean Water Act noted above, in January 2012, an agreement between Pontiac Emergency Manager Lou Schimmel and Oakland County was disclosed that may have resulted in significant loss of funding for the city of Pontiac. At the end of 2011, EM Schimmel signed a cooperative agreement that would let the county receive and administer Pontiac’s share of funds from the U.S. Department of Housing and Urban Development (HUD) for the Community Development Block Grant (CDBG) program through 2014. The problem was it did not legally bind the county to spend the federal dollars intended for Pontiac. After Rep. Peters was alerted that Pontiac would not directly receive HUD funds for fiscal year 2012, Peters asked HUD to review this agreement. Eventually, the City of Pontiac saved up to \$1.4 million according to Rep. Peters’ office.
- Detroit Public Schools -- On December 6, 2010, a Wayne County Court judge ruled that Detroit Public Schools EM Robert Bobb had unlawfully exceeded his mandate by attempting to make academic reforms, which were at that time within the elected school board’s sole discretion. Bobb’s sweeping plan aimed to reform everything from instruction to evaluation processes for staff, most notably by implementing a series of additional standardized tests during the school year. Judge Baxter stated that while the EFM law required Bobb to draft a financial plan to regulate expenditures and investments, the court could not recognize a power that the state legislature did not grant an EFM—in this case, usurping the elected board’s authority over academics and curriculum.

Recommendations

As a result of a review of the factual context surrounding the Michigan EM Law, it became clear that in addition to repealing the statute, a range of action is required by all levels of government and other stakeholders to properly assist those jurisdictions facing severe financial crises. A summary of those recommendations follows:

I. New Legislation is Needed

Relevant stakeholders should work together to amend the EM law to more closely conform to laws in other states which have worked over the years to resolve financial problems and emergencies.

As James E. Spiotto, one of the Nation's leading legal experts concerning financial issues facing state and local governments has explained in his written statement before the Democratic Judiciary Forum, there are numerous instances of non-controversial emergency financial laws which have been consistently used to assist troubled local governments. He concludes, "State and local governments have a history of addressing and solving financially distressed situations." Significantly, none of these laws grant the breadth of unchecked authority or target collective bargaining rights that Michigan's EM Law does. In particular, Mr. Spiotto notes that the state may, through a vehicle such as an intergovernmental cooperation act, refinancing authority or commission step in and provide bridge financing or refinancing of the troubled debt; transfer certain services to other governmental agencies to reduce expenses, and/or grant or loan funds to the municipality to bridge the crisis. Specific legal mechanisms used by other states include the following:

- Debt Advisory Commission (2 states).
- Statutes providing for debt compromise or adjustment process and intercepts of payment (8 states).
- Active technical assistance, grants, loans, budget review (15 states).
- Financial control boards, refinance authorities and active outside supervision and review (23 states).

Examples of the use of these less controversial authorities include the following:

- New York City (1975) – State Municipal Assistance Corporation.
- Cleveland, Ohio (1980) – State bailout to assist in financial restructuring.
- Bridgeport, Conn. (1991) – State enacted special legislation to discipline financing and limit expenditures to actual revenue.

- Philadelphia (1991) – Refinancing and bridge financing as well as restructuring of operation and responsibilities.
- Central Falls, RI (2010) – State enacted law allowing state intervention in the in the form of state oversight of struggling municipalities.
- Harrisburg, PA (2010) – Harrisburg received three state grants for fire protection, and pension assistance and is required to enter state program for a distressed city to prepare a fiscal recovery plan.

Thus, numerous laws in other states have been proven to be effective over the long term and without undermining constitutional and other rights. Michigan should take account of these experiences in crafting new more carefully balanced legislation.

II. A Multi-Pronged Approach is Needed to Respond to the Economic Harm Caused by the Loss of Manufacturing Jobs and the Recession

Michigan's current approach of relying solely on an unelected Emergency Manager (or the threat of an EM) to take over a city's governance and unilaterally cut its budget and eliminate collective bargaining rights is a flawed strategy likely to fail economically, politically, and legally. We recommend a solution providing for a multi-level approach whereby (i) impacted cities work with the private sector and labor to reduce their budgets; (ii) the state reverses harmful budget cuts (including restoring funds obliged to the City of Detroit); and (iii) the federal government enacts and implements legislation designed to assist urban areas with regard to jobs, health care, education, and public safety.

A. Role of Local Governments

Clearly, it is critical for local jurisdictions, including Detroit, to agree to concessions to improve their finances. Mayor Bing is seeking to reduce outlays by more than \$100 million annually, and has negotiated preliminary deals with 49 unions. Considerable work has been placed in these ongoing discussions by the Mayor, City Council, and organized labor. These negotiations are occurring outside of the EM Law.

B. Role of State Government

In recent years, the State of Michigan has routinely enacted a series of significant endless cuts in its budget, which have had a disproportionate impact on cities and the most vulnerable members of society. Cuts in revenue sharing, education and public safety have particularly harmed local governments. As detailed below, Detroit has lost approximately \$220 million in funds previously promised by the state and foregone approximately \$450 million in city income tax receipts.

To further illustrate the revenue loss faced by Detroit as a result of the unilateral actions taken by the State of Michigan, PA 140 of 1971 established Michigan's state revenue sharing scheme, but for more than a decade, Michigan municipalities have watched revenue streams decline, resulting in bare-bone cuts to staffing and the elimination of services on which residents have come to rely. In 1998, State legislators and Detroit city officials passed a measure to shrink the city tax rate for workers (PA 500 and PA 532). The move called for the reduction from 3 percent to 2 percent for Detroit residents and from 1.5 percent to 1 percent for nonresidents. In exchange, legislators agreed not to reduce the money Detroit received in revenue sharing, an expected annual amount of \$339.9 million for the years 1999-2007. It was also agreed in the statute that if state sales and revenues declined, Detroit would be subject to relatively modest reductions in revenue sharing. When sales tax revenue declined, instead of reducing Detroit's payment by \$720,000 in 2007 and \$3.5 million in 2008 as the agreement provided, for example, the state law was changed to reduce Detroit's revenues by an aggregate amount of \$220 million. However, the state did not allow Detroit to increase its income tax, costing the City \$50 million per year, or approximately \$450 million since 2004.

Given the foregoing, it is recommended that legislation be introduced and passed into law requiring the State utilize its most recent projected budget surplus and other revenue sources to comply with its past financial commitments to Detroit as well as other impacted communities.

C. Role of Federal Government

The federal government also has a vital role to play in supporting cities devastated by the twin forces of loss of manufacturing jobs and the most severe economic contractions since the Great Depression. Among other initiatives, the federal government should insure that legislation is in place in the following areas to support financially struggling municipalities:

Jobs/Infrastructure/Housing – Although a variety of measures have been taken over the last several years to combat joblessness, including adoption last week of an extension of the payroll tax reduction, it is clear more needs to be done, including: closing tax loopholes that encourage outsourcing U.S. jobs overseas; providing tax credits to help small businesses hire new employees and sell their products and innovation overseas; and boosting incentives to create American clean energy jobs like making state-of-the-art wind turbines and solar panel. Rep. Conyers has introduced "The Home Foreclosure Reduction Act," legislation that would assist "under water" homeowners keep their homes in bankruptcy, a particular problem in Michigan and other states wracked by Foreclosure (H.R. 1587). Rep. Conyers is also working on legislation that would encourage immigration by those individuals who would bring jobs and investment to Detroit and other urban areas, and has also introduced legislation to provide employment to all Americans, "The Humphrey Hawkins 21st Century Full Employment and

Training Act” (H.R. 870). He has also supported construction of a second bridge from Detroit to Canada and the development of high speed light rail and other transit options for Detroit and its suburbs.

Health Care – Providing for universal, affordable health care is one of the most important things the government can do to assist the many individuals in urban areas who are uninsured. Full implementation of the Affordable Care Act signed by President Obama last Congress will help pursue those ends. In addition, Mr. Conyers has introduced legislation that would provide universal single payer to all individuals, “The Expanded and Improved Medicare for All Act” (H.R. 676).

Education – The American Recovery and Reinvestment Act, signed into law by President Obama, helped mitigate teacher layoffs, and other legislation has been signed into law to make college for affordable for veterans and lower college loan costs, also benefitting urban areas. More needs to be done in the areas of strengthening schools, such as reducing class size, funding special education and rebuilding crumbling schools.

Public Safety – Rep. Conyers is working on initiatives to extend and enhance the Violence Against Women Act and to extend police and other public safety grants to high crime areas facing ongoing budget cuts. Passage of these measures will help our cities insure that citizens are safe in their homes and on the streets.

We appreciate that finding the funds to pay for these various urban priorities will be difficult in the present budget environment. However the cost of neglecting our cities and their residents will be far more in the long run than helping to address their needs in a collaborative manner currently.

III. Greater Oversight of the EM Law is Needed

Enhanced Review of the EM Law and its implementation should be provided by the federal government and the U.S. Congress.

Because of the myriad of problems identified under the Michigan EM Law, including numerous specific instances of abuse, mismanagement and conflict of interest, we recommend that additional and strengthened oversight be provided with respect to the implementation of the law. Unfortunately, that oversight has not been forthcoming at the state level, as the Republicans control all three levels of state government – the Governor’s Office, the State Senate and State House, and the State Supreme Court. Neither Governor Snyder, State Treasurer Dillon, nor any members of the Republican legislative leadership or their designees accepted invitations to

participate in the February 21 Judiciary Forum in Highland Park, nor have they agreed to participate in any of the other public forums held concerning the EM Law.

Given this context, the only possible oversight would appear to be the federal level. To this end, Ranking Member Conyers has asked the Department of Justice to review the Michigan EM Law. As part of that request, we recommend that Rep. Conyers forward the Department a copy of this Report along with a transcript of the February 21 Forum. We would also recommend that Rep. Conyers and other Members forward additional questions and document requests concerning the issues identified in this Report and at the February 21 Forum directly to the Snyder Administration in an effort to obtain a greater understanding of how the EM Law is being reviewed and implemented.

Endnotes

1. See “Michigan’s Hostile Takeover,” MOTHER JONES, available at <http://motherjones.com/politics/2012/02/michigan-emergency-manager-pontiac-detroit>, Feb. 15, 2012.
2. Statement by Professor Kenneth N. Klee for Emergency Financial Manager Town Hall, at 11, 10 (Feb. 21, 2012).
3. Mich. Comp. Laws § 141.1519(k) (2011).
4. Id.
5. Mich. Comp. Laws § 141.1519(j) (2011).
6. Mich. Comp. Laws § 141.1519(k) (2011).
7. U.S. Const., art. 1, sec. 10, cl. 1.
8. U.S. Trust Company of New York v. New Jersey, 431 U.S. 1, 17 (1977).
9. Home Building & Loan Assn. v. Blaisdell, 290 U.S. 398, 431 (1934).
10. U.S. Trust Co. of New York v. New Jersey, 431 U.S. 1, 20 (1977).
11. 290 U.S. 398 (1934).
12. Buffalo Teachers Federation v. Tobe, 464 F.3d 362, 368 (2d Cir. 2006), cert. denied, 550 U.S. 918 (2007).
13. Mich. Comp. Laws § 141.1519(k) (2011)
14. Id.
15. Statement by Professor Kenneth N. Klee for Emergency Financial Manager Town Hall, at 5 (Feb. 21, 2012).
16. Home Building & Loan Assn. v. Blaisdell, 290 U.S. 398, 431 (1934).
17. Id. at 425.

18. Allied Structural Steel Co. v. Spannaus, 438 U.S. 234, 245 (1978).
19. Id.
20. Mich. Comp. Laws § 141.1519(k)(i) (2011).
21. Home Building & Loan Assn. v. Blaisdell, 290 U.S. 398, 425 (1934).
22. Statement by Professor Kenneth N. Klee for Emergency Financial Manager Town Hall, at 8 (Feb. 21, 2012).
23. Mich. Comp. Laws § 141.1519(k) (2011).
24. Association of Surrogates & Supreme Court Reporters v. New York, 940 F.2d 766 (2d Cir. 1991).
25. Mich. Comp. Laws § 141.1519(k)(iv) (2011). The Act provides that (“Any plan involving the rejection, modification, or termination of 1 or more terms and conditions of an existing collective bargaining agreement is temporary[.]”).
26. 11 U.S.C. §§ 901 et seq. First codified in 1934 on a temporary basis in response to the devastating financial impact that the Great Depression had on municipalities across the Nation, Chapter 9 was subsequently made permanent. Pub. L. No. 73-251, 48 Stat. 798 (1934). It was estimated that more than 1,000 municipalities were in default on their bonds. Alan N. Resnick & Henry J. Sommer, 6 COLLIER ON BANKRUPTCY, ¶900.LH[1], at 900-24 (15th ed. rev’d 2007).
27. The Bankruptcy Code defines “municipality” as a “political subdivision or public agency or instrumentality of a State.” 11 U.S.C. § 101(40). Thus, for example, a school district, county, or public agency would be eligible to file for Chapter 9 bankruptcy relief.
28. Alan N. Resnick & Henry J. Sommer, 6 COLLIER ON BANKRUPTCY, ¶900.01[1], at 900-2 (15th ed. rev’d 2007).
29. U.S. Const., art. I, sec. 10, cl. 1.
30. U.S. Const., art. I, sec. 8, cl. 4.

31. 11 U.S.C. § 365. In contrast, Chapter 11 of the Bankruptcy Code (which is a form of bankruptcy relief used by businesses to restructure their financial affairs) has provisions specific to collective bargaining agreements. 11 U.S.C. § 1113.

32. NLRB v. Bildisco & Bildisco, 465 U.S. 513, 526 (1983). The Court also noted that this standard is intended to be “a higher one than that of the ‘business judgment’ rule.” Id

33. 11 U.S.C. §§ 901(a), 1109.

34. Alan N. Resnick & Henry J. Sommer., 6 COLLIER ON BANKRUPTCY, ¶903,01, at 903-2 (15th ed. rev’d 2007).

35. Id. at 901-20-21.

36. 11 U.S.C. § 109(c). To be eligible for Chapter 9 relief, the municipality must be insolvent. 11 U.S.C. § 109(c)(3). Bankruptcy Code section 101(32) defines insolvency with respect to a municipality as a “financial condition such that the municipality is – (i) generally not paying its debts as they become due unless such debts are the subject of a bona fide dispute; or (ii) unable to pay its debts as they become due.” In addition, the municipality must be “specifically authorized” to file for such relief by the state. . Presumably, this requirement would be satisfied by Mich. Comp. Laws § 141.1523 (2011). Other requirements are that the municipality “desires to effect a plan to adjust” its debts. 11 U.S.C. § 109(c)(4). In addition, the Code describes alternative requirements with respect to the municipality’s dealings with its creditors. 11 U.S.C. § 109(c)(5).

37. As amended by PA 4, Michigan’s law provides as follows:

Sec. 23. (1) If, in the judgment of the emergency manager, no reasonable alternative to rectifying the financial emergency of the local government which is in receivership exists, then the emergency manager may recommend to the governor and the state treasurer that the local government be authorized to proceed under title 11 of the United States Code, 11 USC 101 to 1532. If the governor approves of the recommendation, the governor shall inform the state treasurer and the emergency manager in writing of the decision, with a copy to the superintendent of public instruction if the local government is a school district. Upon receipt of the written approval, the emergency manager is authorized to proceed under title 11 of the United States Code, 11 USC 101 to 1532. This section empowers the local government for which an emergency manager has been appointed to become a debtor under title 11 of the United States Code, 11 USC 101 to 1532, as required by section 109 of title 11 of the United States Code, 11 USC 109, and empowers the emergency manager to act exclusively on the local government's behalf in any such case under title 11 of the United States Code, 11 USC 101 to 1532. Mich. Comp. Laws § 141.1523 (2011).

38. Id.

39. The predecessor law to PA 4 provided as follows:

Sec. 22. (1) After giving written notice to the local emergency financial assistance loan board, the emergency financial manager may authorize the local government to proceed under title 11 of the United States Code, 11 U.S.C. 101 to 1330, unless this authorization is disapproved by the local emergency financial assistance loan board within 60 days after the notice has been received by the board. This section empowers the local government for which an emergency financial manager has been appointed to become a debtor under title 11 of the United States Code as required by section 109 of title 11 of the United States Code, 11 U.S.C. 109.

(2) The notice to the local emergency financial assistance loan board under subsection (1) shall include a determination by the emergency financial manager that no feasible financial plan can be adopted that can satisfactorily resolve the financial emergency in a timely manner, or a determination by the emergency financial manager that an adopted financial plan, in effect for at least 180 days, cannot be implemented, as written or as it might be amended, in a manner that can satisfactorily resolve the financial emergency in a timely manner.

Mich. Comp. Law § 141.1222 (repealed 2011).

40. See “Now that the factories are closed, it’s tee time in Benton Harbor, Mich.,” THE NEW YORK TIMES MAGAZINE, available at <http://www.nytimes.com/2011/12/18/magazine/benton-harbor.html?pagewanted=all>, Dec. 15, 2011.

41. Statement of Professor Jocelyn Benson before February 21 Judiciary Democratic Forum.

42. See *Kiernan v. Portland*, 57 Ore. 454, 407 (1910).

43. 394 Mich. 229, 236 (1975).

44. Id.; the Court’s response to the delegation of public responsibilities to private arbitrators: “Where delegation of authority to resolve the dispute to an independent outsider may resolve the immediate crisis and relieves the public employer and union officials of the need to justify the result, this approach to legislative decision-making, precisely because it is designed to insulate and, in fact, does insulate the decision-making process and the results from accountability within the political process, is not consonant with proper governance, and is not an appropriate method for resolving legislative-political issues in a representative democracy.”

45. Mich. Const. Art. III, §2
46. Mich. Const. Art. IV, §29.
47. Mich. Const. Art. VII, §22.
48. MCL 15.261 et seq.
49. See “Detroit’s financial review team work null and void, judge rules,” HUFFINGTON POST DETROIT, available at http://www.huffingtonpost.com/2012/02/15/detroit-financial-review-null-void-judge-william-collette-lawsuit_n_1279111.html?ref=detroit-emergency-manager, Feb. 15, 2012; see also “Judge rules emergency manager process, financial review teams subject to open meetings act,” HUFFINGTON POST DETROIT, available at http://www.huffingtonpost.com/2012/02/02/emergency-manager-financial-review-team-open-meetings-act_n_1249685.html, Feb. 2, 2012.
50. See “Will emergency manager be appointed in Highland Park,” CBS DETROIT, available at <http://detroit.cbslocal.com/2011/12/12/will-emergency-manager-be-appointed-in-highland-park/>, Dec. 12, 2011.
51. See Genellie, Kate. “Auditors: BH still seeing red,” HERALD-PALLADIUM [Southwest Michigan], 7 Jan 2012.
52. See “Now that the factories are closed, it’s tee time in Benton Harbor, Mich.,” THE NEW YORK TIMES MAGAZINE, available at <http://www.nytimes.com/2011/12/18/magazine/benton-harbor.html?pagewanted=all>, Dec. 15, 2011.
53. See “Michigan’s Hostile Takeover,” MOTHER JONES, available at <http://motherjones.com/politics/2012/02/michigan-emergency-manager-pontiac-detroit>, Feb. 15, 2012.

Appendix