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July 31, 2020

The Honorable Detroit City Council  
Coleman A. Young Municipal Center  
2 Woodward Avenue  
Detroit, MI 48226

Re: Revised FY 2020-2029 Long-Term Forecast Report

Dear Honorable Detroit City Council Members:

The Office of the Chief Financial Officer (OCFO) respectfully submits the revised Long-Term Forecast Report for Fiscal Years 2020-2029 completed by the Office of Budget (OB). Since the completion of our initial Report in March, the nation and our city have experienced a dramatic economic slowdown due to the COVID-19 pandemic. The Mayor and City Council acted quickly to address the immediate projected revenue shortfalls for FY2020 and FY2021 with the use of reserves and spending reductions. Through work by several OCFO divisions (including ODG, ODFS, and OB) under the direction of Chief Deputy CFO Katie Hammer, the City will also use federal CARES grants to support all COVID-19 contractual and personnel expenditures, taking pressure off our immediate General Fund crisis.

As a City, we need to not only solve the problem immediately in front of us, but we also must ensure our long-term solvency. The Long-Term Forecast projects a structural imbalance beginning in FY2022, which cannot be solved through reliance on depleted reserves. Instead, Detroit will need to implement restructurings that reduce spending, while continuing to provide the services that Detroiters depend on. OCFO will lead the way in providing a better value to our residents through spending reductions, on which we will update you in the coming months.

While spending smarter will be critical to returning Detroit to balance, the City will also need policies that drive revenue growth. With a revenue structure largely reliant on the success of income tax, structural balance for the City will require policies that drive opportunity to our residents to reduce inequality, attract new residents, and promote new commercial, industrial and residential investment.

Finally, Detroit must continue to plan for our long-term obligations. I look forward to working with the Pension Plan Trustees and Investment Committees to establish a predefined 30-year rolling contributions funding policy with predictable and affordable contributions and less risk to the City and its stakeholders.

Please feel free to contact me if you have questions about the revised Long-Term Forecast Report for FY2020-2029.

Sincerely,

David Massaron  
Chief Financial Officer



# **Long-Term Forecast Report**

**FY 2020–2029**

Office of the Chief Financial Officer  
Office of Budget

Revised: July 31, 2020

# COVID-19 Disclaimer

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- On March 13, 2020, the President declared the ongoing Coronavirus Disease 2019 (COVID-19) pandemic a nationwide emergency.
- On March 23, 2020, Governor Whitmer issued a “Safer at Home” order for Michigan. It was rescinded on June 1, 2020, and the State has begun gradually re-opening the economy.
- On March 30, 2020, the City issued its annual Long-Term Forecast Report, with projections that did not yet reflect the material fiscal impact of COVID-19, to meet the Financial Review Commission’s annual reporting deadline.
- Given the material change in fiscal outlook due to COVID-19, the City is issuing this revised version of the FY 2020-2029 Long-Term Forecast Report.
- This revised report includes updated revenue and expenditure projections based on COVID-19 impacts and changes made in the FY 2021 Adopted Budget.
- This report does not include the additional expenditures for COVID-19 response nor the federal assistance supporting those costs.

# Table of Contents

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Section	Page No.
Legacy Pension Obligations	4
Debt Obligations	12
Long-Term Forecast	16



# Legacy Pension Obligations

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# Legacy Pension Funding Policy

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- The City's legacy pension plans have not yet adopted funding policies
  - Projections in this report assume a 30-year level dollar amortization policy
  - Assumptions are the same as the approved FY 2021-2024 Four-Year Financial Plan
  - Since then, the FY 2019 valuations released in April 2020 indicate another \$12M increase in the projected annual contribution based on final results
  - Poor investment performance for FY 2020 will increase it further
- Recognizing this long-term challenge continues to grow, the City is working with the Pension Plans over the summer of 2020 on a new funding policy
- The City needs greater certainty over its future annual contributions to plan ahead now

# Legacy Pensions Background

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## Plan of Adjustment (POA) Pension Cliff

- POA provided a 10-year “pension holiday” for City to invest in service improvements, capital, and blight removal
- In 2014, POA assumed annual legacy pension contributions increase from \$0 to \$111M in FY 2024 (the “pension cliff”)
- By 2015, updated mortality tables increased unfunded pension liabilities by more than \$490M (34%)
- Updated mortality tables and poor investment performance brought projected annual General Fund contributions to \$166M when the FY 2021 Budget was developed

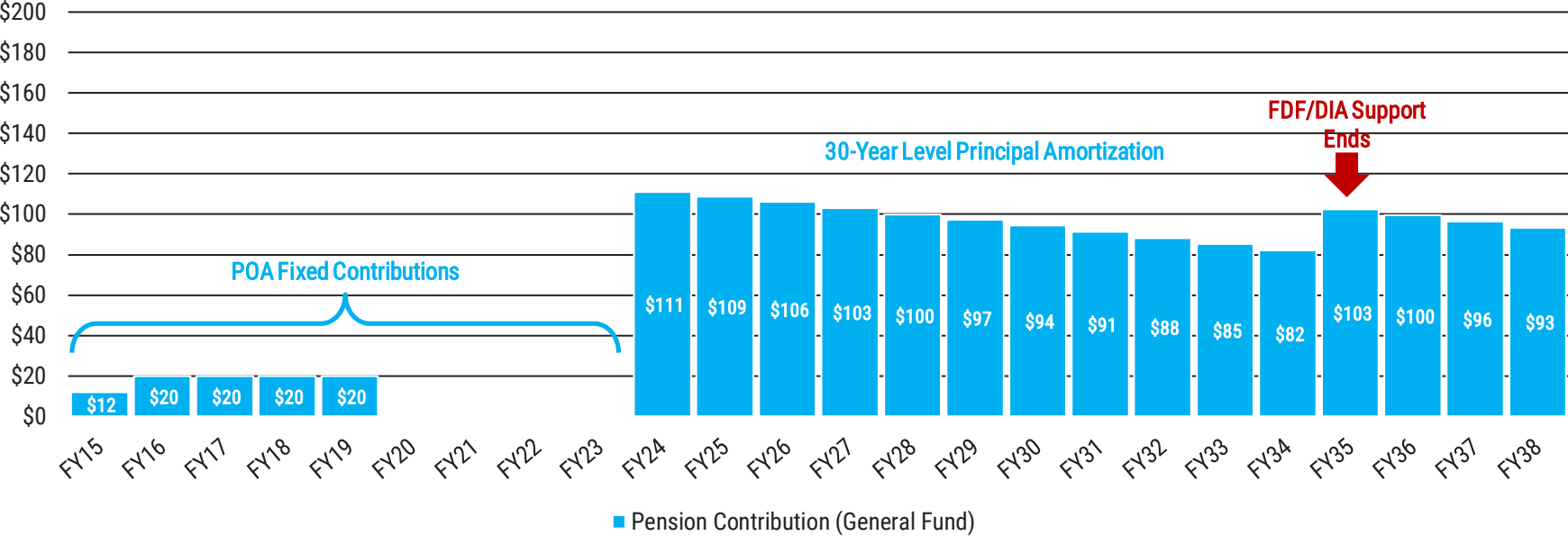
## Retiree Protection Fund (RPF)

In 2017, the Mayor and City Council created the Retiree Protection Fund by ordinance as a long-term strategy for legacy pension funding:

- Provide extra funding for deposit into the RPF, an irrevocable trust for legacy pension obligations
- Use RPF deposits, plus investment earnings, to partially offset annual pension contributions starting FY 2024
- Gradually build up budget capacity for future annual required contributions (the cliff becomes a ramp)
- Review annually and recommend changes if needed during the annual budget process
- To date, the City has deposited \$170M in the RPF

# Plan of Adjustment Requirement (October 2014 Projections)

General Fund  
(\$ in millions)



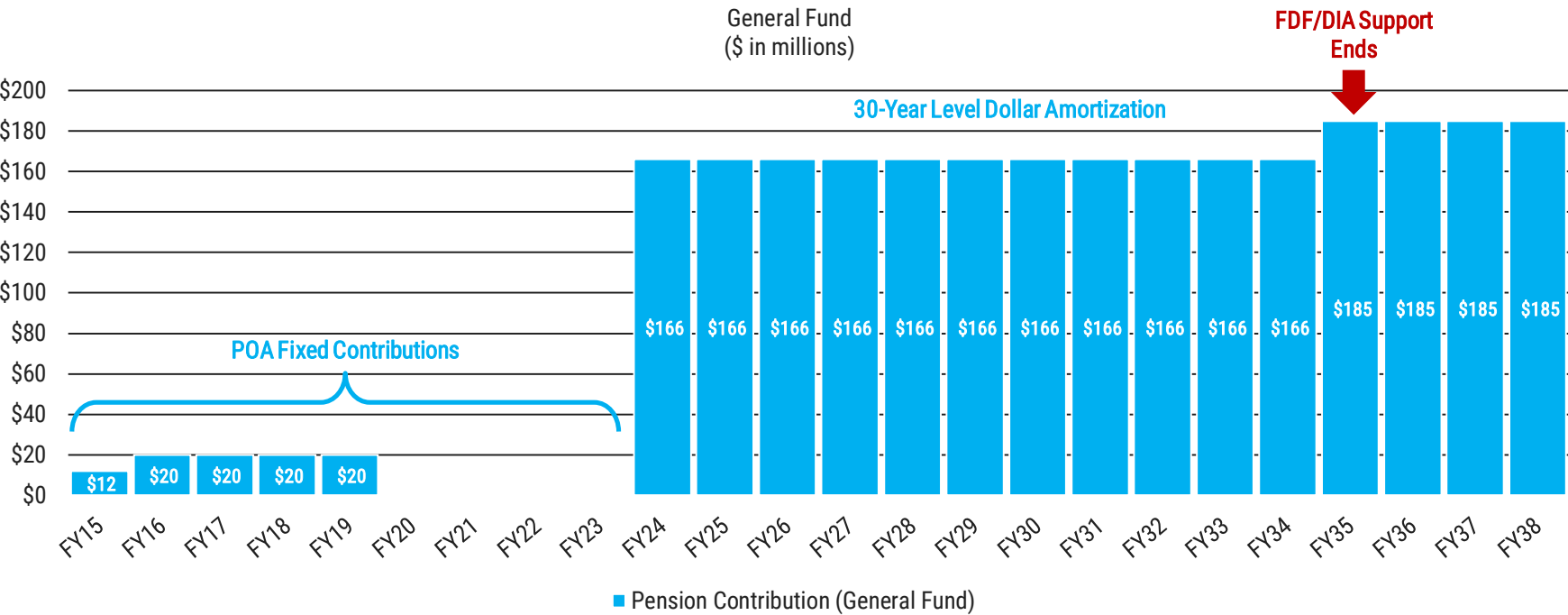
\* Excludes "Grand Bargain" contributions from State of Michigan, Foundation for Detroit's Future (FDF), and Detroit Institute of Arts (DIA). DWS and Library liabilities and contributions are separate.

Projections above based on assumptions at the time of the approved FY 2021-2024 Four-Year Financial Plan. Subsequent plan experience and investment performance will result in larger projected contributions.





# Plan of Adjustment Requirement (with City's March 2020 Projections)

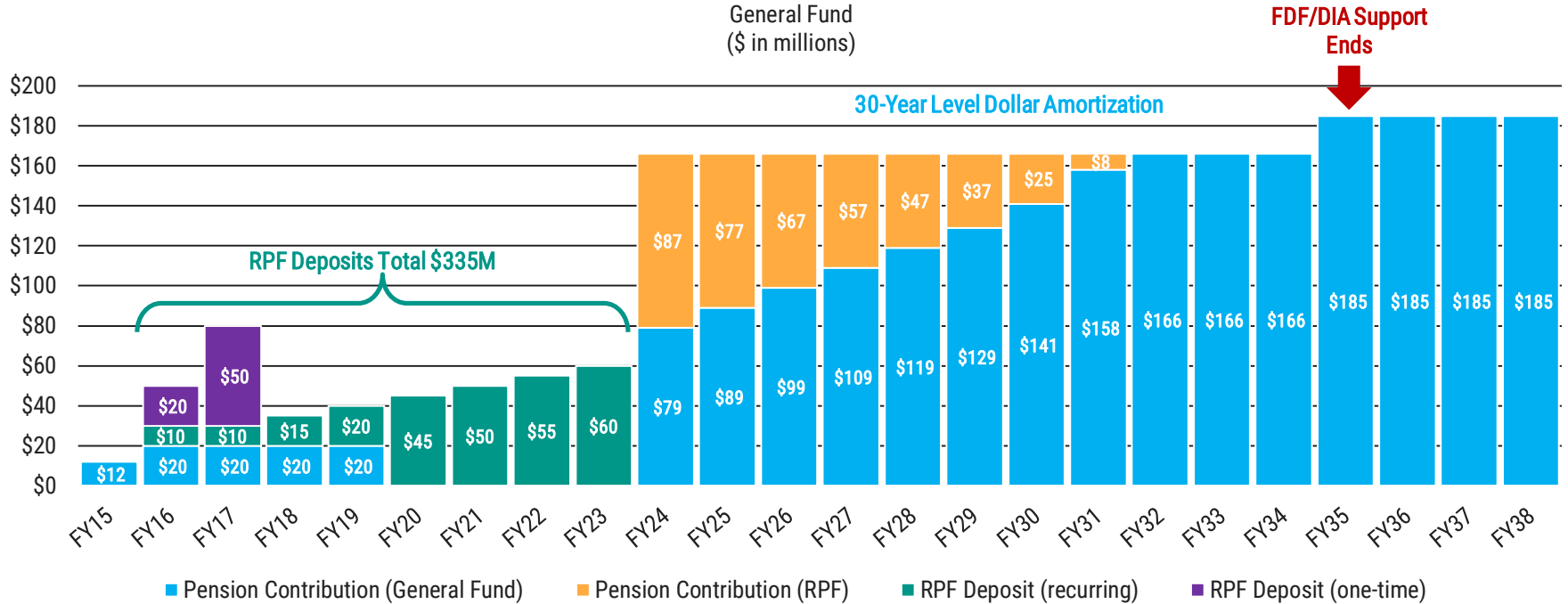


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Projections above based on assumptions at the time of the approved FY 2021-2024 Four-Year Financial Plan. Subsequent plan experience and investment performance will result in larger projected contributions.



# FY 2021 RPF Approved Budget (with City's March 2020 Projections)



\* Excludes "Grand Bargain" contributions from State of Michigan, Foundation for Detroit's Future (FDF), and Detroit Institute of Arts (DIA). DWS and Library liabilities and contributions are separate.

Projections above based on assumptions at the time of the approved FY 2021-2024 Four-Year Financial Plan. Subsequent plan experience and investment performance will result in larger projected contributions.



# FY 2021 Pension Plan and RPF Review

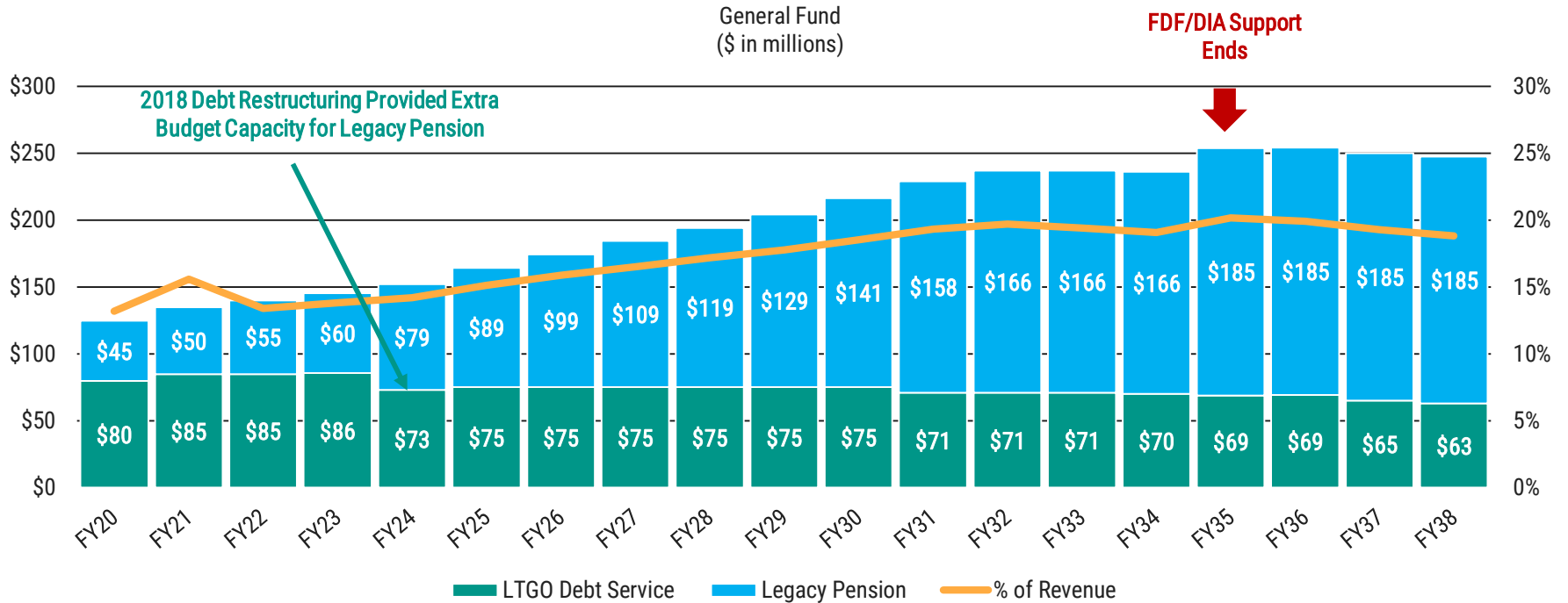
- Prior to developing the FY 2021 Budget recommendation, the OCFO reviewed the latest actuarial valuations, pension plan returns, and RPF returns
- No change to funding policy assumptions
  - Retirement Systems have not yet established funding policies
- FY 2024 net contribution from General Fund increased \$3.5M vs. last year's review
  - Increase driven by pension plan returns below 6.75% target

Pension Model Updates and Assumptions	
Actuarial Valuation <sup>(1)</sup>	FY 2018 valuation
Latest Pension Plan Returns	3.4% GRS, 5.1% PFRS FY 2019 actual return
Future Pension Plan Returns	6.75% projected
Amortization / Funding Policy <sup>(2)</sup>	30-year level dollar
FY 2024 Projected Contribution	\$192M gross <u>(\$26M)</u> FDF/DIA/DWSD/DPL <sup>(3)</sup> <b>\$166M net from General Fund</b>
Latest RPF Returns	4.4% FY 2019 actual return
Future RPF Returns	3% projected

(1) Actuarial valuations for FY 2019 were completed after FY 2021 Budget development.  
 (2) The Retirement Systems have not yet established funding policies  
 (3) Foundation for Detroit's Future and Detroit Institute of Arts are the "Grand Bargain" outside sources through FY 2034. Detroit Water and Sewerage Department and Detroit Public Library pension liabilities do not impact the General Fund.



# Recurring Debt Service and Legacy Pension Costs



Excludes RPF Deposits from one-time fund balance in FY16 (\$20M) and FY17 (\$50M). Excludes "Grand Bargain" contributions, which provide \$18.7M per year through FY34. Excludes DWSD and Library. LTGO Debt Service excludes B-Note debt service allocated to enterprise funds.

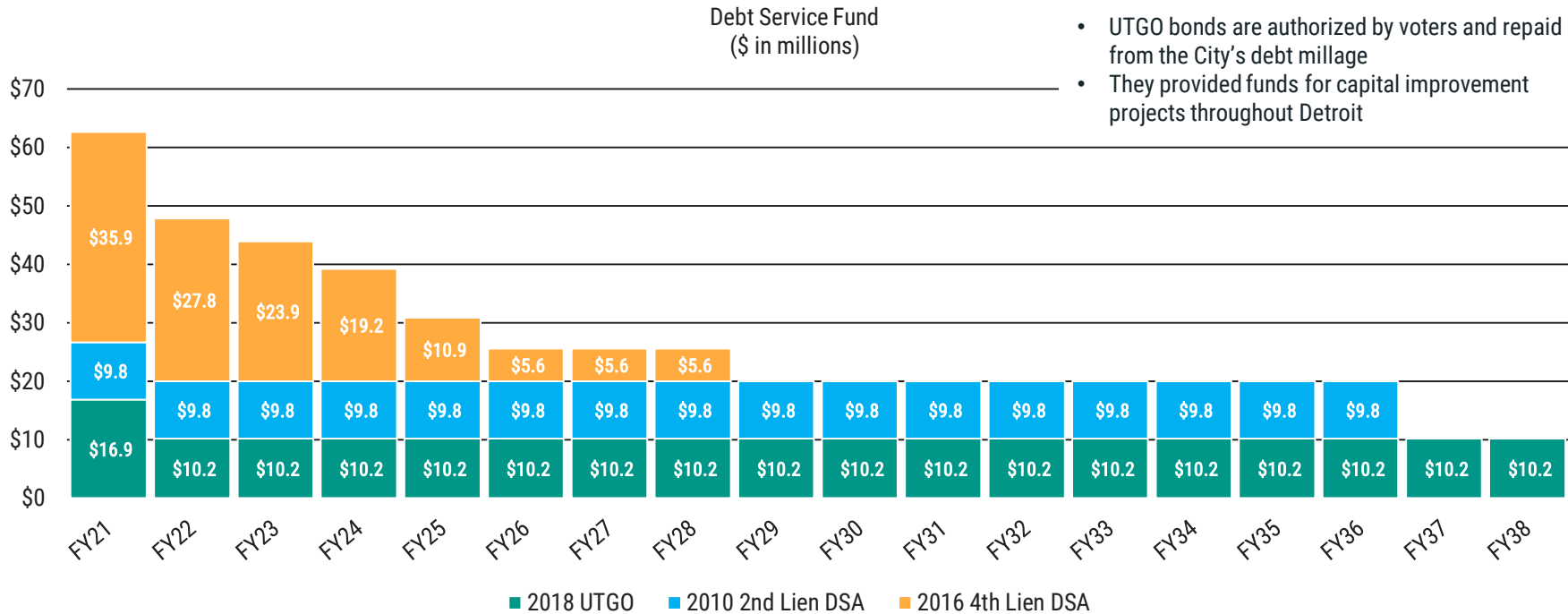


# Debt Obligations

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# Unlimited Tax General Obligation Debt Service



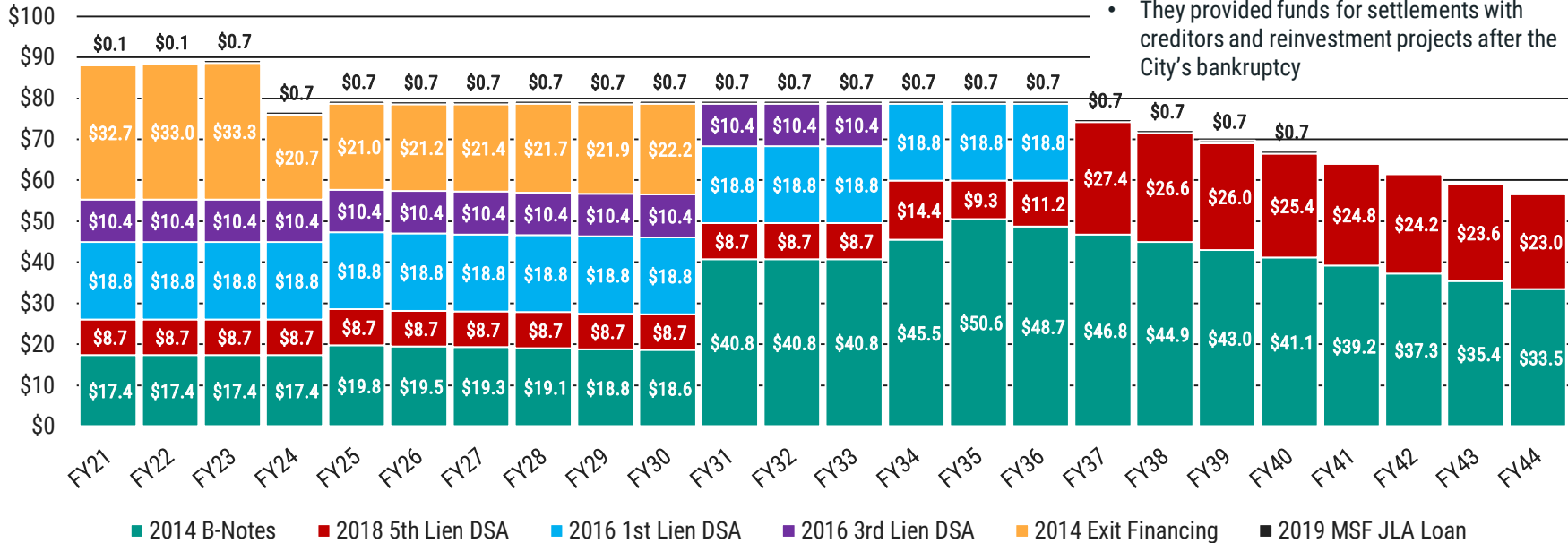
\* Does not include budgeted debt service for next series of previously authorized UTGO bonds.

Source: OCFO – Office of the Treasury



# Limited Tax General Obligation Debt Service

General Fund and Enterprise Funds\*  
(\$ in millions)

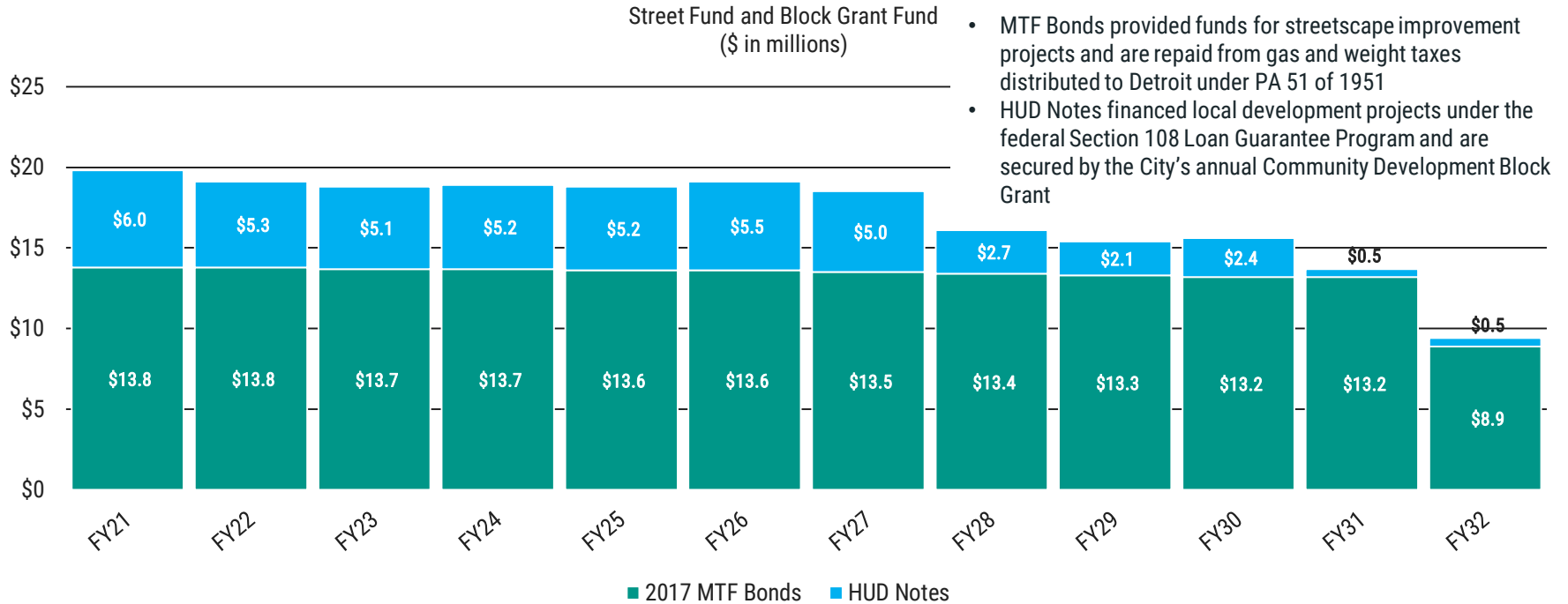


- LTGO bonds are primarily repaid from the City's General Fund revenues
- They provided funds for settlements with creditors and reinvestment projects after the City's bankruptcy

\* 2014 B-Notes are split approximately 80% General Fund and 20% Enterprise Funds. Michigan Strategic Fund Joe Louis Arena Demolition Loan debt service assumes scheduled drawdowns occur.  
Source: OCFO – Office of the Treasury



# Michigan Transportation Fund Bonds and HUD Notes Debt Service



\* MTF Bonds debt service assumes scheduled drawdowns occur.

Source: OCFO – Office of the Treasury





# Long-Term Forecast

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# COVID-19 Impact Summary

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Due to the COVID-19 public health emergency and the measures taken to stop the spread, including stay at home orders, mandatory business closures and impact on the national economy, the long-term forecast assumes substantial revenue losses, most acutely felt in FY 2020 and FY 2021, driven by the following:

- Gaming revenue losses directly tied to the casino closures on March 16, 2020
- Income tax reduction as employers have laid off and furloughed workers and there is a forecasted contraction in the national and state economy
- Anticipated State Revenue Sharing reduction due to a drop in state sales tax receipts
- Other revenue losses from suspended parking enforcement, bus fare interruption to protect drivers from COVID-19 and a reduction in business and construction permitting activity

Consistent with the FY 2021-2024 Four-Year Financial Plan, the forecast assumes fund balance will absorb a portion of the revenue losses in FY 2020 and FY 2021.

# Baseline Forecast Assumptions

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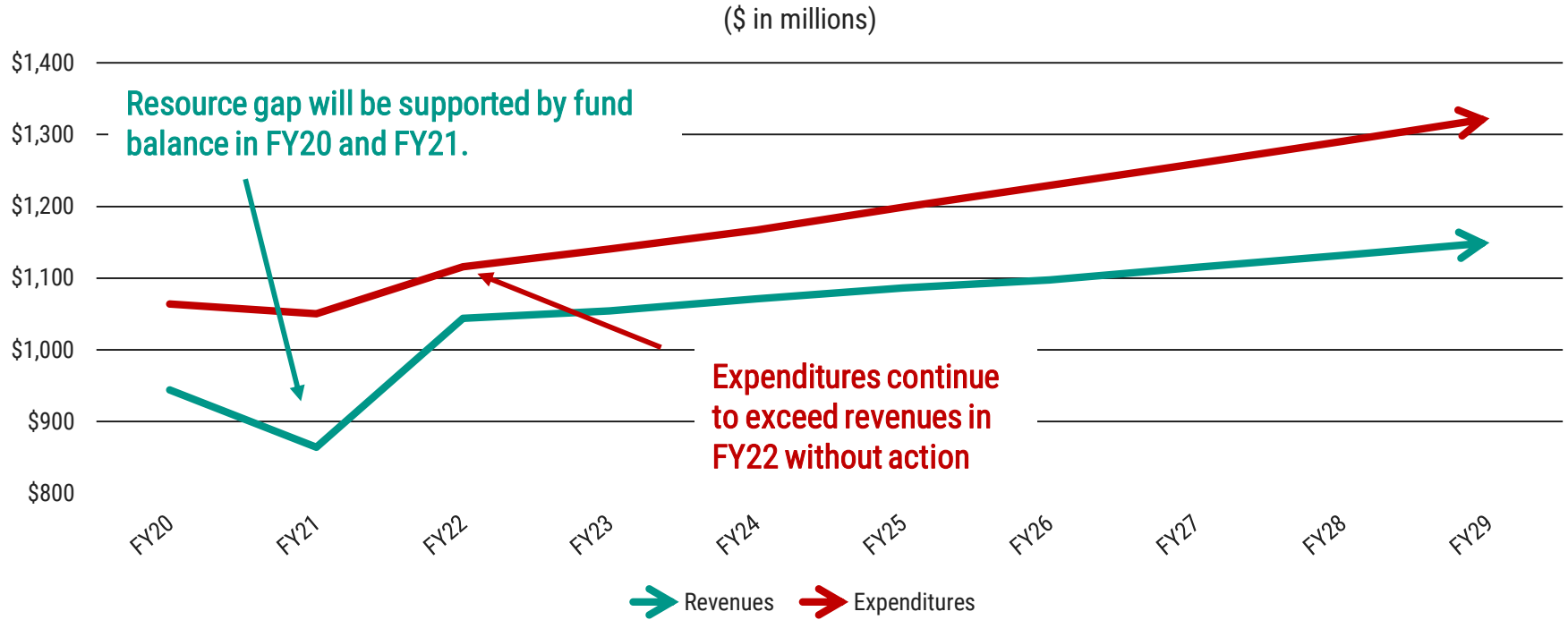
## Revenues

- Based on the City's annual budget for FY 2021 and four-year financial plan for FY 2021 – FY 2024
- Baseline includes additional updates for COVID-19 impacts
- Major revenue growth continues along City budget trends after FY 2024
- Other revenue growth generally held at 2% after FY 2024

## Expenditures (forecasted from FY 2019 actuals and known adjustments)

- Annual wage growth based on current labor agreements and inflationary increases thereafter
- Healthcare, dental, and vision benefits include inflationary growth
- Legacy Pension cost based on FY 2021 Adopted Budget and 30-year level dollar amortization
- Debt service based on existing debt service schedules
- Other operating expenditures include 2% inflationary growth
- Forecast does not include one-time spending from fund balance (e.g., blight, capital, RPF)

# FY 2020-2029 Long-Term Forecast Baseline



\* Includes recurring RPF deposits as expenditures through FY 2023



# COVID-19 Impact Assumptions

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## Income Tax

- Individual tax losses in FY 2020 were estimated using YTD collections through May and a year-end projection
- FY 2021 estimates assume 18.5% annualized US GDP increase in Q3-2020 (initial recovery following Q2 contraction), followed by a slow recovery thereafter
  - Based on the May economic forecast from the University of Michigan, with adjustments for actual City Income Tax experience through May
- Corporate and partnership tax revenue will be flat in FY 2021 and not begin to recover until FY 2022, in line with State revenue expectations
- Assumes additional income tax refunds due to nonresidents working from home due to COVID-19 during FY 2020 and FY 2021, followed by an ongoing 10% loss from a permanent change in remote work behavior
- Assumes a sustained recovery following economic contraction, with no second wave of extraordinary COVID-19 business closures
- While having returned to growth, the City's employment base will remain below prior forecasts

# COVID-19 Impact Assumptions Continued

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## Property Taxes

- Assumes 50% loss in delinquent tax payment plan revenue through end of FY 2020 and for all of FY 2021
- No auction proceeds assumed in FY 2020
- No impact on summer 2020 tax levy, which are based on values as of December 31, 2019
- Does not include potential future impact to taxable values from COVID-19 recession

## Wagering Tax and Fees

- Assumes casino closures through July 31, 2020
- Followed by gradual reopening: Aug-Oct (20%), Nov-Jan (50%), and gradual ramp up from Feb to Nov 2021.
- Casino activity returns to normal or otherwise adapted by FY 2023 to achieve prior forecast

## State Revenue Sharing

- Ongoing annual losses of roughly \$6M for FY 2022-FY 2024 below February 2020 Revenue Estimating Conference
- While having returned to growth, the State sales tax base remains below prior forecasts
- Does not reflect \$24M proposed FY 2020 statutory State Revenue Sharing reduction, which has not yet been enacted, nor potential additional reductions in FY 2021 and forward.

# COVID-19 Impact Assumptions Continued

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## Utility Users Tax

- FY20 losses estimated from YTD collections through May and observed water utility usage.
- Assumes recovery in tax revenue spread between FY 2021 and FY 2022 but will remain below prior forecasts.

## Other Departmental Revenues

- Parking fee and fine losses due to FY 2020 closures and assumed phase-in to normal activity throughout FY 2021
- Court fee and fine losses throughout FY 2020 due to closures
- Loss of license, permitting and inspection charges during closures and economic recession, assumed phase-in to normal activity throughout FY 2021
- Investment earning losses due to economic impacts of COVID-19
- FY 2020 loss in fees and service charges due to closures, such as blight tickets and recreation fees

## Expenditures

- DDOT contribution reduced by \$20 million throughout forecast period per FY 2021-2024 Four-Year Financial Plan
- Removal of FY 2021 general wage increases for non-union employees and bargaining units that have agreed to date

# Risks not included in the forecast

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The City faces continued downside risks not included in the forecast, including, but not limited to:

- Second wave of COVID-19 causing another round of mandatory closures
- Slower reopening of casinos and the local economy than currently expected
- Extended and more severe COVID-19 economic recession
- New normal for economic activity with ongoing capacity limits and remote work
  - Reducing the potential gains from economic development if employment levels are curtailed to meet new capacity limits
- State Revenue Sharing reductions as the State rebalances its budget due to COVID-19 impacts
- Significant growth in annual legacy pension funding contributions if Pension Plans adopt a shorter amortization period and/or continue to fall short on investment performance
- Forecast does not include additional expenditures due to COVID-19 response activities



# Potential upsides not included in the forecast

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The OCFO also forecasts potential revenue and expenditure savings opportunities beyond the baseline for long-term planning purposes **and to drive action to achieve fiscal sustainability:**

- **Economic Growth and Development:** Development projects underway and announced, and gains from expiring Renaissance Zones. Does not assume continued development beyond announced projects. Assumes one-year development delay based on COVID-19.
- **Revenue Enhancements:** Additional aid provided by the federal government, State-shared marijuana excise taxes, internet gaming and sports betting, departmental revenue initiatives (e.g., parking meters and emergency medical service fees).
- **Operational Reform and Efficiencies:** Overtime management, workforce efficiency planning, and potential reductions in actuarially determined hybrid pension contribution rate
- **Eliminate FY 2021 general wage increases or equivalent savings from pending bargaining units:** Provides ongoing savings from eliminating scheduled across-the-board base pay raises (requires labor contract changes), or achieving equivalent departmental savings.
- **Potential federal stimulus for state and local governments.**

# Long-Term Forecast Report

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