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HONORABLE CITY COUNCIL

I am here to present to you the City of Detroit budget for the 2006-2007 fiscal year.

When I came before you last year at this time, there was a lot of talk in the newspapers and elsewhere in this city about the “R” word – receivership.

At that time, I told you that if we did nothing, we would face a \$300 million shortfall in revenues. Many Detroiters continue to ask me if we still have a \$300 million problem. The answer is, “No, we don’t.”

That’s because we did something. We moved forward with a number of initiatives to bring what we spend in line with what we take in.

In fact, for the past four years we have continually implemented efficiencies and made cuts in city operations to bring our budget into balance. When we look at where we are today and compare that to where we were four years ago, the results are dramatic. Those who would have you believe that we have done nothing to bring our budget into balance simply have not been paying attention.

Major reductions achieved

Let me review for you some of the dramatic savings and reorganizations we have achieved in the past four years:

- We have eliminated more than 5,500 jobs from city government, reducing the overall work force by 25.9 percent and the General Fund work force by 39 percent. Four years ago, the City of Detroit had more than 20,000 employees. Today, we have fewer than 15,000 employees.
- We have reduced our gross payroll costs by \$272 million.
- We have laid off 2,400 workers, including police officers and fire fighters.
- We have reduced professional and contractual services city-wide by nearly 24 percent, or \$22 million.
- We have completely reorganized our Police Department.
- We have closed fire stations.

- We have spun off the Detroit Zoo.
- We have spun off the Detroit Historical Museum.
- We reduced the size of our general assigned vehicle fleet by more than 225 vehicles and the use of cell phones so sharply that we have achieved an annual combined savings of \$2 million.
- We have cut General Fund subsidies by \$48 million per year to city enterprise agencies such as the People Mover, the Detroit Zoo and the Detroit Historical Museum, the Parking Department and City Airport.
- We saved \$20 million per year by issuing pension obligation certificates last year.
- We anticipated the rise in natural gas prices early last fall, purchasing and stockpiling supplies of natural gas; in addition we hedged future fuel purchases to lock in lower prices.

These are just some of the reasons Detroit's city government today is leaner than it has been in the memory of anyone alive.

Dealing with structural costs

But we can't just keep laying people off if we want to maintain the core services our citizens deserve and have a right to expect. We can't just keep laying people off if we want Detroit to thrive in the 21st Century. We must dig into some of the structural costs that are built into our budget and bring them under control.

There are six specific areas with substantial structural costs that can, and must, be brought into line: the Department of Public Works, the Detroit Department of Transportation, the Public Lighting Department, the Greater Detroit Resources Recovery Authority and our biggest structural problems – pension and health insurance costs.

We have to rethink the way we operate in each area. We have to become more efficient. We have to bring our employee costs in line with what we can afford and in line with changes occurring in other parts of our economy in the 21st Century. And we have to take steps to assure that earmarked revenues we raise actually cover the costs they are supposed to cover.

A balanced budget

The budget I am presenting to you today does all those things.

To start with, it is a balanced budget. But it is balanced in a way that provides for a level of city services that we need if we are to realize the promise of the Next Detroit at the beginning of the 21st Century. As we prepared this budget, we focused on more than just the coming fiscal year. Based on current economic projections, this budget paves the way for balanced budgets for the next five years.

Those balanced budgets, combined with additional revenues we will realize in four years when we retire some major debt, means we will be in a position where we can actually start carefully and prudently growing and enhancing services as needed. After the past four years of deep cuts, I think you will agree that is very good news.

That plan for a string of balanced budgets is one reason this city is poised for a rebirth. We are poised to create the Next Detroit. For that to happen, city government must be a part of the process, not an anchor holding back progress. This budget makes us part of the process of growth.

Signs of rebirth and growth

Let me give you a few examples of why we can see the Next Detroit on the horizon:

- Last year, for the first time in decades, Detroit led our region in new housing starts. This year, we will more than double that pace and break ground for more than 2,400 new units.
- Our downtown office occupancy in class “A” buildings has been raised to more than 90 percent. And nearly 500,000 square feet of additional office space is under construction downtown with three-fourths of that pre-leased.
- Our entertainment industry is growing. We saw 33 new restaurants open in the last year and our casinos are spending well over \$1 billion to create three permanent facilities that will include 1,200 new hotel rooms downtown.
- Our east riverfront is bustling with activity. Construction continues on the riverwalk, the cement silos are coming down and new residential, office and public space is on the drawing boards.
- Housing prices have risen 46 percent in Detroit in the last four years, compared to 27 percent nationally and 26 percent in the State of Michigan.

There are many more signs of the Next Detroit, but this is a budget message, not a State of the City. I single these out only to make the point that it is critical that we in city government make the decisions necessary to assure that Detroit's government in the 21st Century is as state-of-the-art as the exciting growth and development we see around us.

New initiatives to streamline government

You will see in this budget new initiatives to streamline existing city services such as building maintenance and security that now are spread out among different agencies in a very inefficient pattern.

You will see in this budget a reflection of labor and management working together to get cost reductions in health care and other costs that have become badly out of sync with the world around us.

You will see in this budget an initiative to bring the cost of delivering trash pickup services in line with the revenues needed to support that service.

You will not see in this budget "if-come" items like the kind we put in the budget for the current year such as moving towards spin-offs of the Zoo and Historical Departments. We eventually got those done. But it took us almost until the end of the budget year to get them done. This budget is not dependent on "if-come" items that will take the year to work out.

You will not see substantial additional layoffs, either. This budget envisions only 77 layoffs in total, with largest number in any department being 11 layoffs at Cobo Hall.

The initiatives in this budget are all designed to improve our services to our citizens. The past four years, frankly, have been a continual rush to battle when it came to dealing with our budget. We faced soaring deficits, with huge gaps every year beginning the day we walked into the job. Every year we had to struggle to balance our budget.

Our challenge today is to change the structure of city government to produce the quality city services that people deserve and want while continuing to drive down costs to the citizens. We want to lower property taxes. We want to get back to reducing our city income tax, which already has been reduced to 2.5 percent for residents and 1.25 percent for non-residents. We want to make our departments more effective and more efficient. This budget is designed to move us in that direction.

Working together

Before I get into the highlights, I also want to speak personally to each member of this Honorable Body. Today is the beginning of the process where we will work together to produce a new budget for the 2006-2007 fiscal year.

I will be reaching out to each of you throughout this process. Following my message today my office will be in touch with each of you to schedule an individual meeting between you and me and key members of our budget and finance staff. Our goal will be to answer your questions and share whatever information you desire.

I also want the people of Detroit to know that we will be going out and having budget meetings throughout the city of Detroit in the coming weeks just as we went out into the neighborhoods for conversations last year.

I am determined to make this process work for this Honorable Body, this City and the people of this City. I am determined to give Detroiters the modern, efficient and effective government they have a right to expect at the beginning of the 21st Century.

Trash collection

No issue has received more attention in recent weeks than the issue of trash collection. In the current fiscal year we eliminated monthly, curbside bulk trash pickup in the City of Detroit, saving approximately \$20 million for our general fund – the equivalent of about 250 police officers. I made that choice in the belief that most Detroiters would rather eliminate bulk pickup than lay off an additional 250 police officers.

In my State of the City message, I mentioned trash collection and disposal as one of the services that we needed to review to determine how it should be delivered and whether it required city employees to deliver it. We followed that up by contacting private contractors and looking at their pricing compared to our current costs. We found that for us, at this point in time, it didn't make cents – that's c-e-n-t-s.

Today, switching to a private contractor would not produce a savings in cost or a greater service than what we have now. It may be that in 2009, when the bonds expire on the Greater Detroit Resource Recovery Authority facility, the picture will change. But for now, the financially prudent decision is that trash collection should remain a city service delivered by city employees.

At the same time, we must change the way we pay for trash collection and disposal. Since 1976 Detroiters have paid a three-mill property tax that is earmarked for trash collection and disposal. This year those three mills raised \$28 million. Unfortunately, it costs us a little more than \$100 million a year to actually collect and dispose of trash in the city of Detroit, even after the elimination of bulk trash. That's about \$75 million in general fund revenue that is required to cover the additional cost – the cost of nearly 1,000 police officers.

Other communities, both in our immediate area and around the nation, who have faced a similar dilemma have gone to a "fee for service" approach to cover the cost of trash removal. That means charging a separate fee to cover the actual cost of the service being delivered. The City of Atlanta, Georgia has done this. Our neighboring community of Southfield has done this. Other communities have done this.

This budget calls for a residential trash collection fee of \$75 per quarter, or \$25 per month, per household to help finance the cost of trash collection in Detroit. The fee will be billed and paid quarterly. There will be provisions for a 30 percent reduction in the fee for qualifying senior citizens and other limited income households. Our calculation is that 70 percent of seniors will qualify for the discount. The three-mill trash collection levy will be eliminated from your property tax bill. That lowering of the property tax will help produce an increase in property values in the city.

Even this quarterly fee will not fully cover the cost of trash collection and disposal. Our calculation is that with 280,000 households in this city, after allowing for discounts for seniors and delinquencies, it will raise \$67 million per year. That's a net of almost \$40 million more than the three mills currently being levied. While it won't cover the full cost of trash disposal, it will provide desperately needed additional funding tied directly to this specific service that will free up \$40 million in General Fund revenues to go elsewhere.

I recognize that there will be considerable debate over this proposal. I have given it very thoughtful consideration as we formulated our plan. It grows out of the reality that if we are going to maintain a basic level of city services and if we are going to live within our means, like every Detroit household what we spend must match what we take in. This is one area where the revenue stream originally developed to cover the cost – the three-mill property tax – long ago stopped being enough to cover the cost of the service it was intended to pay for.

I urge your Honorable Body to give this very careful consideration before you reach any conclusions. We stand ready to provide you all of the information that we have pulled together as we have formulated this plan.

Controlling illegal dumping

This budget also includes an aggressive effort to clean up and bring an end to the illegal dumping of trash that plagues our neighborhoods. I understand and share the concern of Detroiters that there is too much dumping in our city, in our neighborhoods and in our right of ways.

I've heard the suggestions of some that the end of bulk trash pickup has somehow worsened the problem of illegal dumping in Detroit. I would remind you of two things. The first is that this is Michigan, and every year this is the dirtiest time of the year throughout the state as winter departs and spring arrives. That is why we have spring cleaning.

Secondly, you may remember that last year in April, when we still had bulk trash pickup, we had more bulk trash piling up than ever. We had to call in special contractors to come clean up the city of Detroit. So illegal dumping and the accumulation of trash was a problem even with bulk pickup.

Instead of going back to bulk pickup, we need to aggressively target those who trash our city by illegally dumping in our city. This budget creates 33 additional positions in the Department of Public Works to be devoted to a full-time program to clean up illegal dump sites. Our expectation is that most if not all of those 33 positions will be filled by calling back laid off DPW workers. We also are linking our 311 call-in system with DPW so that citizens who see illegal dumping can report it immediately to a single location.

With a specific operation targeted solely to illegal dump sites, we will be able to clean them up much more efficiently. Today we have a backlog of more than 300 illegal dump sites that need to be cleaned up. This new task force will enable us to attack that problem. Part of the problem with these illegal dump sites is that we let them stay there too long because we don't have the resources within our department now to pick it up. Once a pile is there, sometimes even good people do bad by throwing trash on top of an existing pile. We must get rid of the illegal dump sites now.

As your Mayor, I pledge that we will clean up this illegal dumping situation. We are going to begin this effort to clean up our city in the month of May with our 2006 Motor City Makeover. But I need your help. We are asking all of our neighborhoods to participate. We are asking all of our businesses to participate. We are asking all of our citizens to participate. We want to scour this city clean.

Then, we are going to coordinate our Code Enforcement Task Force with DPW to step up enforcement actions against those who dump illegally in our city.

Starting June 1st, we are coming with the most aggressive code enforcement and anti-illegal dumping effort ever. Those who dump illegally show their contempt for Detroit and the people of Detroit. Illegal dumping is a crime. We will treat violators accordingly. There will be visible signs, there will be an intense public information effort and there also will be sting operations with media partners to help us catch, draw attention to and punish those who are illegally dumping.

As a unified community we must all be committed to keeping our city clean. We cannot and we will not bring back or create any initiative that promotes citizens putting trash out on our streets that is not in a Courville container. Putting trash on the curb is not the answer. Picking up the trash in our right-of-ways and in our communities and in our vacant lots is the answer.

The only way we can afford to do all this is to move, as other communities have, from a millage-based system to a fee-based system, with a fee that is earmarked to pay for the specific service. So I urge you to carefully consider this plan to clean up our city and to help fund that clean up with a fee targeted specifically for that purpose.

General Services Department

A key part of our plan to cut costs and make our operations more efficient is the creation of a General Services Department for the City of Detroit. This department will manage functions such as security services, janitorial services and inventory management throughout city government.

The General Services Department will be the maintenance department for all of our city buildings and property, will coordinate security services for all city facilities and will consolidate our inventory management into one system.

We have completed a city-wide review of these functions and found that we are extremely inefficient in all of them. One of our most inefficient areas is inventory management. We found we have more than 100 different contracts for purchasing a wide variety of parts with 66 different vendors. We found no effort to coordinate or leverage those contracts to provide savings for the City.

The Fire Department literally still has a manual system where people write on a piece of paper what they have in inventory. Consolidating our inventory control will put all of these activities together under the direction of individuals who actually have an expertise in inventory systems.

We also found that we are spending far too much money on security and janitorial services. We have 15 or 16 different security contracts, all with different rates, in different city departments. The same is true for janitorial services – we have contracts with a lot of different companies at a lot of different rates. The new General Services Department will enable us manage these contracts in a much more efficient and effective manner.

We anticipate a savings in the first year of some \$1.7 million from consolidating and managing inventory and contracts and an additional savings of \$2.9 million through attrition as workers retire or resign and do not need to be replaced because of our increased efficiency.

Human Resources Management System

One of the ways to become more efficient is to assure that we have up to date technology in place to help us manage basic city services.

Our current payroll system is 29 years old. In technological terms, that is prehistoric. The system is totally incapable of meeting our needs in 2006. It has no time capture component. We don't know how long people work in city government. We don't know when they go to lunch. We don't know when they go on vacation sometimes.

We must make sure we better manage our time and our costs within those systems. Last year I proposed, and Council approved, \$25 million for a new Human Resource Management System. The new system will make sure we are capturing the time of our employees, capturing the proper cost of employees, paying people what they deserve and operating a modern 21st Century payroll system. It will more than pay for itself through the efficiencies it will enable us to achieve. We purchased and are implementing that system through financing from GE Capital. This budget includes \$7.4 million to service that debt.

Police officer recalls

Last fall when we announced that we were laying off 150 police officers, I said that most or all of them would be back within a year. Today I am announcing that the chief is sending out the first callback letters this week to 30 officers who have been laid off. By June 30 of this year we expect to have called back a total of 100 of the laid off officers to fill vacancies created by retirements.

Once all of those who were laid off have been called back, we will begin recalling the student police officers who were in the Training Academy last year when we had to lay them off. We have cut our department back as far as we can prudently cut. As vacancies occur, we will continue to fill them.

10 percent pay cut

Last year's budget also included a one year, 10 percent pay cut for all city employees. I voluntarily took the cut immediately in March. So did all of my appointees. Our city non-union employees took the cut beginning July 1.

Earlier this year, the Public Attorneys Association, representing the attorneys in the law department, became the first bargaining unit to accept the 10 percent pay reduction for one year as well as changes in health care benefits. I want to publicly thank union President Phil Brown and the PAA for taking a leadership role in this effort. We are still seeking to secure that reduction from our other bargaining units and have budgeted the reduction from July 1st through June 30th.

Since my appointed staff took their one year cut beginning last March, the 10 percent cut will end for them on May 1. Our non-union workers will revert back to their original salaries August 1st. As other bargaining units agree to the 10 per cent cut, each agreement will last only one year.

I've always said I wouldn't ask anybody to do anything I wouldn't do. While my year is up as well, to show my commitment to this cut, I will continue to voluntarily take the 10 percent reduction until everybody else's cut has expired and every city employee is back to full salary.

Transportation

As many of you know, our DDOT system is the only one of the 24 largest transit systems in the nation that does not charge a fee for physically disabled riders. New York, Chicago, Philadelphia, Boston, San Francisco, Portland, Oregon and all the other systems charge a fee. The suburban SMART system charges a fee for physically disabled riders. The fare helps cover the cost of the service to the individual. It also recognizes that being physically disabled does not in and of itself mean an individual is financially disabled.

In most systems, the fare is set at one-half of the full fare. That is what this budget proposes – a fare of 75 cents for disabled riders that will raise approximately \$3 million annually to help pay the cost of DDOT.

We have made tremendous strides in improving the quality of service to the disabled and to all riders on the DDOT system over the past year. Our ridership in January, February and March of this year was up a total of 1.5 million riders over the same three months of 2005, a clear indication that people are finding the system more reliable and are using it. This modest fare is an equitable way to raise additional funds to help fund a system that will still require \$75 million from our General Fund this year.

Let me be clear, seniors will still ride free. The new fare will be paid only by disabled riders.

We also have to start working toward developing an effective regional transportation system if we are to move this city and this region forward.

It is absurd that we have the SMART system with more than 400 buses and the DDOT system with more than 400 buses and yet people are still waiting for buses. We need a cooperative regional operating agreement. We need to make regional transportation a reality in this city and this region.

The simplest problem to solve should be bus service. But we need to focus on more than just bus service. We need to be talking about rail – high-speed rail; center city loops; getting from the airport to the central business district. I am committed to solving that problem this year. It's not in this budget, but there will be teams aggressively working on this. As we make progress, we will keep this Honorable Body up to date on our progress.

Property sales

This budget also anticipates \$30 million from property sales, a reduction from this year's budget. Those of you who were here last year will remember that when I proposed \$40 million in revenue from property sales, some members of this body were skeptical. Some members said that it would never be attained, that we would never get anywhere near that amount because it had never been done before. I am pleased to inform you that to date, we have sold or have commitments to purchase \$36 million in property.

This year we are developing whole new strategies, including bundling of properties as well as looking at the assets of city government that can be sold and placed back on the tax roles.

Recreation Centers

We are pursuing two strategies at the same time for those recreation centers that the city must close. For some we will partner with non-profit organizations and churches to take over the recreation responsibility at a center. The center will remain a city owned facility, but our partner organizations will keep it open for the community and bring their constituency base to some of these centers that otherwise would be left empty.

The other is to sell a few of our recreation centers to private developers who will actually put them back on the tax roles. We will be delivering a plan to you this year that includes the sale of everything from recreation centers to land near golf courses for new housing. For instance, at River Rouge Park we have four parcels that developers want to build houses on around the golf course, creating a golf course community. The result will be more new housing in Detroit, a vibrant new community in Detroit and new land and homes on our tax roles.

One of our ongoing problems is that we have an infrastructure that originally was designed to accommodate two million people but now have fewer than one million in the city. Proposals such as the sale of strategically selected land and closed facilities are a creative way to make good use of land that now is lying dormant and breathe new energy into our community. We are conducting a thorough review of these proposals now and will be coming back to the Council once we have a solid recommendation to put before you.

Pensions and health care

We continue to face serious challenges in trying to gain control of the cost of pensions and health care.

In the past four years, our pension costs have shot up more than 175 percent, from \$48 million to a projected \$133.6 million in the coming fiscal year.

Health care is even more costly. In the coming fiscal year alone, we project a 20% increase from the \$184 million we spent in the current year to \$218 million in 2006-2007. It would be even higher -- \$48 million higher -- were it not for savings that we are negotiating with our unions and that we have secured from our providers.

That projected cost includes an assumption that labor and management will successfully work together to achieve badly needed cost reductions in health care. We have been at the bargaining table with our largest civilian union -- AFSCME -- for the past year seeking agreement on a new Alternative Health Care Plan. The plan will increase employee co-pays to levels that reflect the realities of the workplace in this new century.

At the same time, we continue to seek an agreement to accept the one-year 10 percent pay cut that appointees, non-union workers and city attorneys already have taken. I remain confident that we will be able to achieve an agreement.

But I want you to know that if we can't reach an equitable agreement, I have the legal authority to impose our last best offer. If necessary, I will do that. I would much rather come to a meeting of the minds so we can work this out together with our unions. But I am committed to bringing these costs under control. We have been negotiating for the past year and now we are in fact-finding. One way or another, this will be resolved in time for the new budget.

I also today want to touch on two other initiatives that we will be working on over the year that you won't see reflected in this budget because we didn't want any "if-comes" items in it. But these are two areas for which we will find solutions this budget year.

Public Lighting Department

The first area is our Public Lighting Department. Clearly, we need to make the department more reliable. Public Lighting's reliability has been a frustrating problem for me and for mayors before me. With much of its infrastructure dating back to early in the last century, it has defied a solution. I can no longer tolerate our citizens and our city being in the dark. I am determined to solve this problem this year.

At the moment, we are looking into partnering with someone else to make the system more reliable. That does not necessarily mean selling the asset. It does mean reaching out for alternative solutions that we cannot do by ourselves. We are not a power company. We'll be communicating with you and the citizens of Detroit on that process as we move forward. My goal is for the lights to be on. My pledge to you is that they will be on and we will have a solution for this community.

Greater Detroit Resource Recovery Authority

We also will be working this year to determine what the City should do when we pay off the bonds for the Greater Detroit Resource Recovery Authority in the 2008-2009 Budget Year. This budget includes \$85 million to cover payment on the bonds, the operation of GDRRA and the land filling of the ash produced from the 800,000 tons of trash that is burned each year at the facility.

We will be looking at what it would cost to continue operating the facility compared to what it would cost to return to land filling our waste without incinerating it. That review will include determining what it would cost to keep the facility up to date, what the impact would be on the landfill market if an additional 800,000 tons of waste were inserted into the market, how customers of GDRRA could continue to receive the steam heat that it now produces and other issues. We will have a recommendation by this time next year.

To give you an idea of what paying off the GDRRA bonds means, this year's bond payment totals \$79 million. The final GDRRA bond payment, in the 2008-2009 fiscal year, will be \$46 million. Combine that with the fact that in the same year we will make the final payment of \$40 million on our fiscal stabilization bonds. That means we start the following fiscal year with an additional \$86 million right off the top. So you can see why I am convinced that if we can hold the line on spending and continue to improve our productivity and efficiency, our future holds much promise.

A thoughtful and responsible budget

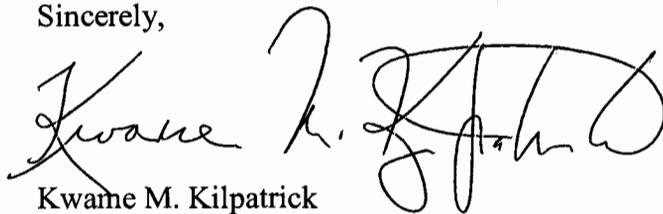
As you conduct your review of this budget in the coming weeks, I believe you will find it is a thoughtful and responsible approach to setting the foundation for the Next Detroit.

It builds on the tremendous progress we have made in the past four years in cutting back on our costs to bring them in line with our revenues. It provides a more realistic revenue stream to meet those basic services that we must provide for our citizens. It continues the progress we have made in modernizing a governmental structure that is still in many areas stuck in the middle of the 20th Century. And it continues the transformation of Detroit city government into an entity that will nurture the growth of the Next Detroit.

When the history of this era is written you and I will be judged on whether we had the political will to make the tough decisions and the smart decisions to put this city in a position to thrive in the 21st Century. I believe this budget meets that test. I look forward to working closely with your Honorable Body in the coming weeks as we finalize the City Budget for fiscal 2006-2007.

Thank you.

Sincerely,

A handwritten signature in black ink, appearing to read "Kwame M. Kilpatrick". The signature is fluid and cursive, with a large initial "K" and a stylized "M".

Kwame M. Kilpatrick
Mayor, City of Detroit