



April 12, 2007

HONORABLE CITY COUNCIL

I am here to present to you the City of Detroit budget for the 2007-2008 fiscal year.

The budget I present to you today is a balanced budget. In fact, this budget will be our third budget in a row that is structurally balanced – meaning what we spend lines up with what we take in.

In addition, this new budget completes the process of paying down the accumulated deficit we have been carrying over from previous years. On June 30, 2008, we will have completely eliminated our deficit.

When I came into office our finances were grossly out of focus. The first year I was here we had a \$69 million deficit. Then it grew to \$96 million, then it grew to \$155 million my third year.

I'm sure you remember that just two years ago we faced a potential deficit of \$300 million. There was a lot of talk about Detroit being on the brink of receivership. There was a lot of talk of bankruptcy. Structural costs that we had inherited were killing us.

To deal with our structural costs we had to do painful things:

- We laid off employees, reducing our overall city workforce from more than 20,000 to now just over 15,000.
- We cut our contracts by 43 percent.
- We closed police stations.
- We closed fire stations.
- We laid off police officers.
- We initiated a trash collection fee.
- We transferred operations of the Detroit Zoo, the Detroit Historical Museum, and Eastern Market to nonprofit organizations.
- We negotiated a 10 percent pay cut with our civilian employee unions.
- We negotiated increases in health care deductibles and co-pays with those same civilian employee unions.
- Just recently, we also were able to win critical adjustments in health care costs from our uniformed employees through an Act 312 arbitration ruling, for the first time securing co-pays from them.
- We did not refinance any of our debt. Instead, we stayed disciplined and worked to eliminate it.

We are now realizing the fruits of these often difficult cuts. What is particularly important is that they are permanent savings that will be a continuing part of our budget for years to come.

For instance, with the changes we have achieved in health care benefits, we have reduced our health care costs by \$35 million per year. That's a savings of \$35 million in the current fiscal year, the coming fiscal year and years after that.

Many people sitting here on this council made the tough decision to change last year from a millage based system for trash collection to a fee-based system. We now are collecting about \$74 million in trash fees where the old three-mill levy was only picking up \$27 million a year. That's another \$47 million annual savings for our General Fund.

When you look at the results we have achieved over the past five years we have achieved a tremendous reduction in our expenditures. Salaries and wages are down by almost \$80 million, or 16 percent, compared to five years ago. Contractual services are down by 43 percent compared to five years ago. Operating expenses are down 20 percent compared to five years ago.

Just think about that for a minute. In each of these areas, we are spending substantially less than we did five years ago. How many other governmental units can make that same statement? I believe that underscores just how serious we have been about bringing our expenditures in line with what we take in. I believe it underscores how well we have managed our way through this very critical problem.

As I did in my State of the City message, I want to thank all of the men and women who serve as our city employees and our retirees for recognizing the situation we face, coming together with us and accepting the changes that had to be made in wages and benefit levels.

I should add here that we still have one piece of unfinished business that we committed to in our current budget. In the budget that we adopted for the current fiscal year, we said we would sell \$30 million worth of property. Thus far we have achieved one-third of that goal. We must complete the rest of those sales in this fiscal year.

I saw a comment recently from Peter Karmanos, who said of budgets, "It's not fun work."

I think we all would agree with that observation, particularly when times are tight. But it is important work. It is part of the heavy lifting of responsible public policy.

I want to acknowledge today the key role that City Council has played in helping make all of these changes.

I particularly want to acknowledge the smooth budget process that we were able to work through last year. In my message to you last year I pledged to reach out and work individually with each of you to answer your questions and share whatever information you desired. The result was a healthy, deliberative process that produced constructive agreements to deliver basic services to our citizens. Council made some very tough decisions along the way. I believe the people of Detroit were well served by the process and I want to publicly thank this Honorable Body for your actions.

I make the same pledge to you again today. My staff and I stand ready to answer your questions, to share whatever information you desire and to work with you in a cooperative manner to continue the remarkable progress we have achieved.

I am pleased that in spite of the belt tightening that we have had to undergo in recent years, we have not neglected our core services. We have opened the first new recreation centers in 20 years. We established a single point of entry into the health care system for our senior citizens. We have invested more than \$100 million in upgrades in our public safety technology. We installed new computerized fare boxes in our DDOT buses. We are investing \$14 million in the Northwest Activity Center that will make it a full community center.

We also see signs of hope and progress all around us. In 2006, Detroit once again led the region in new residential building permits, issuing almost 500 of them. The redevelopment of our riverfront continues to gain momentum.

The Book Cadillac renovations are well underway with all but four of the 67 condo units planned for the upper floors already sold, two of them for more than \$1 million. Another development team that bought the air rights on top of the parking deck being built next to the Book Cadillac already has sold more than half of the 80 upscale condominiums they will put on top of that garage.

MGM Grand Detroit and Motor City Casino will open their new permanent casinos, complete with 400 room hotels, later this year. Greektown will open their new facility next year. MGM has begun hiring more than 1,000 new employees to staff its expanded operations.

Next month we will launch our Next Detroit Neighborhood Initiative (NDNI), a five-year strategy focusing on the rejuvenation of Detroit neighborhoods. This initiative has been greeted with great enthusiasm by neighborhoods eager to be involved in the renewal of this great city. It will concentrate on improving such basic quality of life issues as cleanliness, safety and beautification through growth and development strategies. It is the biggest neighborhood initiative that Detroit has ever seen.

We have started out by targeting our resources to six neighborhoods across this city because we cannot do all 139 square miles of this city at once. Each of the six neighborhoods in our initiative has developed and submitted its own individual work plan. Our City departments are aligning their focus to our Next Detroit Neighborhood

Initiative as well. We'll roll out our final plan for each neighborhood in the middle of May and begin work immediately.

But this is a budget message and my focus today is our budget – both what we have done to bring it under control and what we must do to continue the prudent course upon which we have embarked. We have come a very long way in a relatively short time.

This administration has brought a new discipline to the way we develop our budget.

The budget process starts each year with each department director submitting a proposed budget for his or her department for the new fiscal year. Those departmental submissions often have been unrealistic wish lists that we could never afford. Department directors threw a lot of things at the wall to see if something would stick. It was true under Dennis Archer. It was true under Coleman Young. It was true long before either of them became Mayor.

But this year the initial submissions from our departments were much more disciplined and in line with reality. In fact, they totaled only \$80 million more than the budget I am presenting to you. It was a far cry from years past when departmental requests exceeded well over \$300 million beyond what was possible.

I believe that reflects a much more professional, much more realistic approach to management on the part of all of our department directors. It shows that they are advocating on behalf of their departments, but that they are doing it in a way that recognizes the larger reality and the constraints within which we must work. I want to thank each of my department heads for their willingness to work constructively within this process.

I am pleased to tell you that the budget I present to you today has no layoffs. As we continue to refine our operations, there will be some position changes in various departments. But no one is going to lose their job because of this budget.

The budget I am presenting to you today includes several key initiatives designed to build on the progress we have made.

Our number one responsibility as a city government, of course, is public safety. In my State of the City message you may remember I announced my intent to hire 200 new police officers in the coming fiscal year. Of that total, 94 will be hired to fill openings due to attrition. The remaining 106 officers will fill new positions added in this budget.

Sixty one of those officers will be assigned to the department's new rapid response units that are being piloted in two of our districts and will soon be rolled out citywide. They will be assigned strictly to respond to priority 911 calls and will be

strategically located to assure that any call can be responded to quickly. These are high visibility, directed patrols that will significantly improve our ability to respond quickly to emergencies.

Forty one of the new positions will be funded with drug forfeiture funds, lessening the impact on our General Fund.

One of our more significant successes in the current fiscal year was restructuring our residential solid waste collection. I referred earlier in this message to the solid waste fee we adopted last year to cover part of the cost of residential trash collection. This budget extends that system to commercial trash collection as well, eliminating the three mill trash collection tax on businesses and replacing it with a commercial solid waste fee.

Businesses that do not have a licensed contractor handling their solid waste will have the option of using three different sizes of city container for their trash. They will be charged for each container that they use.

By ordinance, DPW is required to verify that every business that does not use DPW has an appropriate level of solid waste service provided by a licensed contractor. This budget also institutes an inspection fee for all businesses to make sure they have made arrangements for trash disposal service, whether it is a private contractor or the City.

The fee is minimal, ranging from \$150 up to as high as \$1,000 per business. It will pay for the cost of conducting inspections to make sure every business has an appropriate level of service. Every business operating in this city has a responsibility to take care of its own trash. This inspection program is designed to make sure that happens.

Solid waste disposal provides an excellent example of the way we have systematically brought our costs in line with our revenues. In the 2005-2006 budget the General Fund subsidy for solid waste collection and disposal was \$75 million. When we adopted a solid waste collection fee of \$300 per household this fiscal year it allowed us to lower our General Fund subsidy to \$43 million.

In the new fiscal year with the new commercial fee the General Fund subsidy will be reduced once again to \$21 million. In fiscal 2008-2009, when we finish paying off the bonds for the Greater Detroit Resource Recovery Authority, the General Fund cost for trash disposal will be zero. Let me repeat that – in fiscal 2009 there will be no General Fund subsidy for trash collection. It will be totally self-supporting. That means in a period of four years we will have gone from \$75 million in General Fund money to no dollars from the General Fund for trash collection and disposal. This is an outstanding example of how we have managed and brought these costs under control.

Because of all the steps we have taken to bring expenditures in line with revenues we're on a much better footing to stay balanced in coming years.

I said at the beginning of my message that on June 30, 2008 we will be completely out of debt.

We began the last fiscal year, the 2005-2006 fiscal year, with a carryover deficit of \$155.4 million. At the end of that fiscal year, the deficit had grown by only \$200,000. That's a \$200,000 gap out of a \$1.5 billion budget.

That is what you call balancing operations. I've sat in this chair and we've been \$69 million off, we've been \$95 million off, we've been \$155 million off. Today, we're \$200,000 off on a \$1.5 billion budget.

Standard & Poor's, which is the bond rating agency that had us one step away from non-investment grade, said last year that if we could accomplish a series of goals, we would move to a stable rating. They didn't believe that we could do it. Not only have we accomplished all of those goals, including securing health care savings from both our civilian and uniformed employees, we have moved beyond. Last week when the bond rating agencies were in to meet with us, they applauded the work we have done and were fascinated that we have done so much in so little time.

In previous years we've come to this council with a laundry list of things we've had to get done to solve a deficit problem. We've said we were going to work a miracle. Today, because we continue to stay focused and work together, we don't need a miracle to eliminate our accumulated deficit. We just need execution.

There are only three things we need to cure the current deficit. First, you will remember that in our current budget we set aside \$67 million to be applied to the deficit. We have achieved that goal. For the first time, funds we have appropriated to pay down the deficit actually are being applied to the deficit. That will bring it down to \$88 million.

In the new budget, we earmark another \$30 million to reduce the deficit. Every week we are managing better on a wide variety of fronts in city government and keeping our costs under control. That means we can reduce the deficit by another \$30 million with the savings we will achieve in the next fiscal year.

The third thing we are going to do is to execute a long-term deal on the Detroit-Windsor Tunnel. As you all will recall, last year we had a lease agreement for the tunnel for \$20 million and we had a check in hand. But after completing our due diligence, we found that by working with the City of Windsor, we can gain more dollars.

We are preparing to enter into a \$75 million deal with the City of Windsor for a 75-year joint operations and use agreement of the Detroit-Windsor Tunnel. We've made a conservative estimate and have only booked \$58 million of that for this budget because there will be a number of costs and fees associated with finalizing the lease agreement. But that \$58 million will be enough to eliminate our deficit.

We'll be coming back to Council with all the information about the proposed tunnel lease and will be prepared to answer all of your questions once the details are completed.

This budget continues our efforts to streamline city operations. In fact, as you examine this budget you will note that our General Fund expenditures are actually projected to be reduced \$27 million from the current fiscal year.

This budget creates a central system for ordering and keeping an inventory of vehicle maintenance parts. Currently, our vehicle maintenance operations are spread among a variety of departments – DPW, Fire, Police and others – with no adequate coordinated controls on inventories. We have a lot of old parts or parts that were incorrectly purchased that are sitting on shelves gathering dust.

Our General Services Department has issued a request for proposal seeking a single contractor that will manage our entire inventory of parts for fire trucks, police cars, DPW trucks and other vehicles.

We believe this will have a very positive impact on productivity by streamlining the repair process. Without the right parts a lot of vehicles stay out of service longer than is necessary. A central system for parts management will result in more efficient repair of our vehicles and allow them to be back in service much quicker.

The City of Chicago has implemented a similar program and has realized dramatic efficiencies. Prices for the most frequently needed parts dropped an average of 27 percent. The time mechanics had to wait for parts dropped by 40 percent. Savings through rebates and warranty recoveries increased. And the contractor guaranteed that 80 percent of the parts that were needed would be available on demand. We need that system here.

This budget also implements a plan to centralize our accounts receivable operations within the Finance Department. Historically, many of our departments have been responsible for issuing and collecting fees for such activities as inspections, rental of city property, and other activities. There has been no central management of the process and a lot of fees have not been collected. I, as well as this Honorable Body, have been tremendously concerned about our revenue and fee collections.

Now, we are going to get rid of these individual collections units within departments and centralize these activities to Finance. This will be a phased transition spread out over a couple of years. The first year we will be consolidating billing and collections for Fire, DPW and the Department of Administrative Hearings. The following year we will add the Civic Center, the Recreation Department and Building and Safety Engineering departments. The result will be that we do a much better job of collecting what is owed to the city.

We also are instituting a one-time amnesty program for delinquent personal property taxes.

Last year we collected only 77 percent of personal property taxes that were due. We must do better. As a part of that effort, we will institute the amnesty program to allow those who have fallen behind to get caught up in their taxes. We anticipate \$8 million in revenue from the amnesty program.

Once the amnesty period is completed, we will begin strong enforcement actions.

Let me emphasize that this is a one-time program. We have decided that we're not doing amnesties any more. This is the last time we will do an amnesty program. I'm urging all Detroit to take advantage of this.

This budget also adds 10 positions to the Human Rights Department to conduct compliance audits for the Detroit Business Certification Program. These new employees will audit companies to make sure they are meeting the requirements of their certification. They also will be auditing Detroit-based companies to assure that they are properly withholding city income taxes. These 10 positions will generate enough revenue to pay for themselves.

This budget includes an energy management services agreement that will increase Public Lighting Department revenues by \$5 million. Under the agreement we will sell excess energy from the Mistersky Power Plant to other utilities when we do not need it ourselves.

This budget restores to our civilian workforce the 10 percent pay cut that they took during the current fiscal year as part of our budget stabilization plan. We committed to these employees that we would restore their pay. It is time to follow through on that commitment, a step that will cost us \$11 million.

This budget also includes \$8 million for the Recreation Department from funds paid to the city by our three casinos as a result of the renegotiation of their development agreements that we completed in 2002. These payments are in addition to the wagering taxes paid by the casinos. When we reached that agreement, we committed that when the payments began a portion of them would be earmarked for the Recreation Department. This budget allocates \$4 million for capital improvements and another \$4 million to hire seasonal workers to staff rec centers during the busiest months.

I have to add here that you may remember the criticism we received from some detractors when we finished those renegotiations. They claimed we had struck a bad deal.

Well, as a result of those negotiations we have a new \$800 million casino under construction, a \$500 million casino under construction and a \$400 million casino under construction. We will have 2,000 more casino jobs than we have now. Our wagering tax

revenues have almost doubled. We took title to property that is critical to our redevelopment of the riverfront without having to pay back the \$150 million the city had borrowed from the casinos to purchase the land in the first place. And we set up a \$40 million economic development fund, \$5 million of which is going to help build the first African American business and cultural district in the City of Detroit. This development, which started out as African Town at this table, will be the new Paradise Valley.

In this new budget, four of our five major sources of revenue -- property taxes, income taxes, casino taxes and the utility user tax -- are projected to be up by a little more than \$25 million in total. I believe this reflects the new energy that we see in Detroit as we work to create the Next Detroit.

The only source that is projected to be down is state revenue sharing, with a reduction of \$8 million -- a reflection of the difficult times the State of Michigan continues to experience. The real danger to this budget is the State of Michigan. We have endured nine cuts in our revenue sharing funds totaling \$56.6 million in less than six years. We're hopeful there will be no additional cuts this year.

I believe this budget I am presenting to you today is a "good news" story. We have brought a discipline to our budget process that many skeptics did not believe was possible just a few years ago.

If we continue to manage our costs, if we continue to keep a close eye on every expenditure, then we can keep telling this story. We can continue to have a situation where we don't need additional layoffs. We can sustain our bond rating with Wall Street.

But if these costs get out of line even a little bit it threatens our ability to continue to tell the good news story. We have no margin for error. We are just balancing our operations. There is no big pot of money. There is no surplus.

I look forward to working with you 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 moving this City forward. It reflects the tremendous progress we have made working together to put this city on a firm financial footing. And it offers measured initiatives to build on the progress we have made.

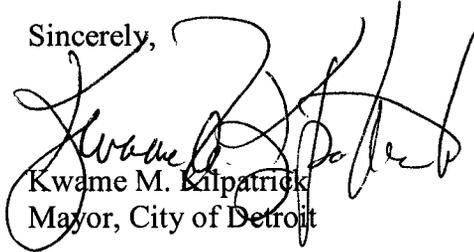
When we look back over the past five years it is clear we have made tremendous progress in cutting our costs to bring them in line with our revenues. No one is talking about receivership for Detroit today. No one is talking about bankruptcy for Detroit today. Instead, we hear talk of progress, of new development and of a new pride that is manifesting itself in our neighborhoods, along our riverfront and in our downtown.

This budget is a reflection of that progress and that pride. This budget is a reflection of the Next Detroit.

I look forward to working closely with your Honorable Body in the coming weeks as we finalize the City Budget for fiscal 2007-2008.

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 "M".

Kwame M. Kilpatrick  
Mayor, City of Detroit