STATE OF MICHIGAN
IN THE SUPREME COURT

MICHIGAN ASSOCIATION OF HOME BUILDERS; ASSOCIATED BUILDERS OF CONTRACTORS OF MICHIGAN; and MICHIGAN PLUMBING AND MECHANICAL CONTRACTORS ASSOCIATION, Michigan Non-Profit Corporations,

Plaintiffs-Appellants,

v.

CITY OF TROY, a Michigan Municipal Corporation,

Defendant-Appellee.

Supreme Court No. 156737

Court of Appeals Case No. 331708

Oakland County Circuit Court
Case No. 10-115620-CZ

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THE MICHIGAN MUNICIPAL LEAGUE'S, THE MICHIGAN TOWNSHIP ASSOCIATION'S AND THE GOVERNMENT LAW SECTION OF THE STATE BAR OF MICHIGAN'S AMICUS CURIAE BRIEF IN RESPONSE TO THE COURT'S JUNE 20, 2018 ORDER

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DESCRIPTION OF AMICI CURIAE

The Michigan Municipal League ("MML") is a non-profit Michigan corporation whose purpose is the improvement of municipal government and administration through cooperative effort. Its membership is comprised of 524 Michigan local governments, of which 478 are also members of the Michigan Municipal League Legal Defense Fund (the "Legal Defense Fund"). MML operates the Legal Defense Fund through a board of directors. The purpose of the Legal Defense Fund is to represent the member local governments in litigation of statewide significance. This amicus curiae brief is authorized by the Legal Defense Fund's Board of Directors, whose membership includes the president and executive director of MML, and the officers and directors of the Michigan Association of Municipal Attorneys: Clyde J. Robinson, city attorney, Kalamazoo; John C. Schrier, city attorney, Muskegon; Lori Grigg Bluhm, city attorney, Troy; Eric D. Williams, city attorney, Big Rapids; James J. Murray, city attorney, Boyne City and Petoskey; Robert J. Jamo, city attorney, Menominee; Thomas R. Schultz, city attorney, Farmington and Novi; Lauren Trible-Laucht, city attorney, Traverse City; Ebony L. Duff, city attorney, Oak Park; Steven D. Mann, city attorney, Milan; and Christopher Johnson, general counsel of the MML.

The Michigan Township Association ("MTA") is a Michigan non-profit corporation whose membership consists in excess of 1,230 townships within the State of Michigan (including both general law and charter townships) joined together for the purpose of providing education, exchange of information and guidance to and among township officials to enhance the more efficient and knowledgeable administration of township government services under the laws and statute of the State of Michigan. The MTA Board of Directors has authorized and directed this

office as attorneys for the MTA to file this amicus curiae brief in support of the Defendant-Appellee the City of Troy ("City") regarding the issues in this lawsuit.

Finally, the Government Law Section of the State Bar of Michigan ("GLS") is a voluntary membership section of the State Bar of Michigan, comprised of approximately 692 attorneys who generally represent the interests of government corporations, including cities, villages, townships and counties, boards and commissions, and special authorities. Although the Section is open to all members of the State Bar, its focus is centered on the laws, regulations, and procedures relating to public law. GLS provides education, information and analysis about issues of concern to its membership and the public through meetings, seminars, the State Bar of Michigan website, public service programs and publications. GLS is committed to promoting the fair and just administration of public law. In furtherance of this purpose, GLS participates in cases that are significant to governmental entities throughout the State of Michigan. The Section has filed numerous amicus curiae briefs in state and federal courts. The GLS Council, the GLS decision-making body, is currently comprised of 21 members. The filing of this brief was authorized at a July 20, 2018, special meeting of the Council held in accordance with Section 6.2 of the Council's Bylaws. A quorum of the Council was present at the meeting (13 members), and the motion passed by a vote of 11-0 with two abstentions. The position expressed in this amicus brief is that of GLS only and is not the position of the State Bar of Michigan.

PROCEDURAL BACKGROUND

On December 27, 2017, MML, MTA and GLS filed an amicus curiae brief in support of the City's answer to the Plaintiffs' application for leave to appeal. In its June 20, 2018 Order, the Court asked the parties to brief several additional issues prior to oral argument on whether to grant the Plaintiffs' application for leave to appeal. In the June 2018 Order, the Court also invited MML, MTA and GLS to file this second amicus brief, which is being filed in accordance with the time limits set by Michigan Court Rule 7.312(H)(3). Per the Court's June 2018 Order, amici curiae do not restate the issues raised in their December 27, 2017 amicus brief, but they do incorporate those issues by reference.

SUPPLEMENTAL ARGUMENT

The State of Michigan's legal framework regarding municipal financing and borrowing provides important context for this matter. As the Court is aware, municipalities like the City may only exercise the powers that are conferred upon them. See *Hess v Cannon Township*, 265 Mich App 582, 590; 696 NW2d 742 (2005) ("While the provisions of the Constitution and law regarding counties, townships, cities and villages must be liberally construed in their favor, the powers granted . . . by the Constitution and by law must include only those fairly implied and not prohibited by the Constitution."). The Michigan Constitution has provided municipalities with fairly broad power to regulate their own affairs. See MML, MTA and GLS December 27, 2017 Amicus Curiae Brief at 4-6. However, municipalities have no inherent or implied right to borrow money. The Michigan Constitution explicitly circumscribes a municipality's power to borrow money to that bestowed by the Michigan Legislature:

> The legislature shall provide by general laws for the incorporation of cities and villages. Such laws shall . . . restrict the powers of cities and villages to borrow money and contract debts. . . .

Const 1963, Art VII, §21.

In turn, the Michigan Legislature, via the Home Rule City Act, permits municipalities to "provide for the borrowing of money . . . for any purpose within the scope of the powers of the city," but limits the method of borrowing to "issuing bonds." MCL 117.4a(1). This proscription on municipal borrowing is further underscored by the Michigan Legislature in the Revised Municipal Finance Act, which governs the issuance of municipal securities. Under the Act, municipal securities are limited to those debt instruments that are issued by a municipality and pledge payment of the debt by the municipality. See MCL 141.2301 ("A municipality shall not issue a municipal security except in accordance with this act."); MCL 141.2103(r) ("'Security' means an evidence of debt such as a bond, note contract, obligation, refunding obligation, certificate of indebtedness, or other similar instrument issued by a municipality, which pledges payment of the debt by the municipality from an identified source of revenue.").

All of this simply means that municipalities like the City cannot stroll down to the local bank and borrow money to finance municipal operations. Instead, if municipalities want to borrow money from a third party, they must issue bonds to do so. Moreover, municipalities may only issue bonds for limited purposes, usually (but not always) to finance projects and public improvements or to fund capital improvements. See, e.g., Revised Municipal Finance Act, MCL 141.2101 *et seq.* (financing of certain projects and capital improvements); Revenue Bond Act, MCL 141.101 *et seq.* (financing of self-supporting public improvements); Municipal Sewage and Water Supply Systems Act, MCL 124.281 *et seq.* (authorizing municipal authorities to issue bonds to acquire and/or construct sewage disposal, water supply or solid waste management

systems); Downtown Development Authority Act, MCL 125.1651 *et seq.* (financing of improvements in the DDA's Downtown District). Municipalities can also issue tax anticipation notes to provide funds for capital or operating expenses in anticipation of tax revenue. See Revised Municipal Finance Act, MCL 141.2101 *et seq.* But no law permits a municipality to issue securities to cover deficits in **fee** revenue, let alone borrow money from a bank or other party to cover the same.

Municipalities do, however, have the legislative authority to "levy and collect taxes for municipal purposes" (MCL 117.3(g)), and to annually appropriate money for "municipal purposes" (MCL 117.3(h)), provided such authority is included in the municipal charter. Thus, municipalities are free to use general tax fund dollars for their own purposes. In this case, Troy (like many other municipalities) has adopted a charter that authorizes the levy of a general tax to raise the revenue "it shall deem necessary to defray all expenses and expenditures set forth in the budget and to pay all the liabilities of the City." Charter of the City of Troy, §9.16 (Tax Levy; Limitations). This provision allows Troy to use general fund tax dollars to cover the deficits experienced by its municipal departments, including its building department.

It is not unusual for governmental entities to use general fund dollars to pay expenses incurred by municipal departments. This is because municipal budgets are good faith estimates of what municipalities expect revenues and expenditures to be, not guarantees. Municipalities spend a great deal of time and effort in the budgeting process, reviewing actual costs from the prior year and relying on prior years' actual revenues and expenses to determine what to anticipate for the coming year. When budgeting for a particular department, a municipality must consider a host of factors including, but not limited to, the direct and indirect costs of the service being provided by the department, the demand for the service being

provided, the overarching economic climate, and whether any assessed fee will be robust enough to cover the costs of service but affordable enough to ensure payment and encourage, not stifle, the use of the service. If a municipality errs in its analysis of any one of these factors, the actual revenue recovered by the municipality could be significantly less than what was budgeted, thereby triggering the need for general fund revenue to fiscally fortify the department. The delicate balance that a municipality must maintain when establishing a budget for services (and a corresponding fee) may in part be the reason why the law often requires fees to be "reasonable" and not "exact" or "precise" or "perfect."

It is also not unusual for a department to then reimburse the general fund for expenses covered on its behalf – whether in the same fiscal year or over several fiscal years through a repayment plan. Although sometimes these reimbursements occur within the same fund (as is the case here with the City, which reported its building permit revenue in its general fund), these reimbursements and repayments may also happen between funds (e.g., from a departmental or enterprise fund to a general fund). In fact, the State of Michigan expects that transfers and loans between municipal units will occur. See, e.g., *What to Look for in Audit Reports: Fundamentals of Understanding Governmental Audit Reports*, Michigan Department of Treasury, p. 4 (recognizing that audit reports may include "[b]orrowing from other funds of the local unit (interfund transfers)" and "[l]oans to other funds."). These transfers are so customary that the Governmental Accounting Standards Board has policy statements and standards on the subject. See, e.g., Statement No. 38 of the Governmental Accounting Standards Board ¶¶15, 60-65 ("Interfund Balances and Transfers"); see also Summary of Statement No. 34 ("Interfund activity includes interfund loans, interfund services provided and used, and interfund transfers. This activity should be reported separately in the fund financial statements and generally should be

eliminated in the aggregated government-wide financial statements."). However, transfers need not be between funds and may be "intrafund," as evidenced by the audit reports for the Michigan State Legislature, whose agencies are funded by the State's general fund. See https://www.house.mi.gov/PDFs/Financials/AuditReportFY2015-2016.pdf at 2. These reports reflect "intrafund" reimbursements that "represent monies transferred to agencies within the Michigan Legislature from other State of Michigan agencies external to the Michigan Legislature, but included in the General Fund of the State of Michigan." *Id.* at 6. This is no different than the City reporting within its general fund the reimbursements made by departments who provide non-general fund services but happen to report their revenues in the general fund.

In short, it is not unlawful for a department to repay monies borrowed from the general fund, which is essentially what the City is doing with respect to its building department revenue. As noted in the City's Comprehensive Annual Financial Reports, which have been independently audited by Rehmann Robson for the last decade, the City is spending what the Plaintiffs have called "surplus" building department revenue to reimburse the general fund for monies previously advanced to the building department by the general fund (not to pay for activities unrelated to the building department). This type of reimbursement between departments and/or funds is entirely consistent with the way municipal borrowing works in Michigan. Because a municipality cannot obtain a bank loan to cover shortfalls and because a municipality cannot issue bonds to cover deficits in fee revenue, the municipality must rely on its charter authority to use its general fund dollars to cover whatever expenses are incurred to serve its purposes – whether it be to supply clean drinking water, to maintain public health by treating sewage and hauling solid waste, or to ensure the safe construction of homes and non-residential structures.

In this regard, a municipality operates a business enterprise and is, at times, no different than a commercial business.

This Court has concluded that with respect to the operation and management of a business enterprise, a municipality "has the same right and power to do those things connected with the operation of such business as would a private corporation." *Nelson v Wayne County*, 289 Mich 284, 296-97; 268 NW 617 (1939). It should be permitted to make these business decisions, and unless there is obvious deception or clear mismanagement at play, the judiciary need not interfere with these decisions:

> The power to engage in [] municipal business activity for the public welfare is necessarily conferred in general terms. **To go into details of administration and specify each particular thing which could or could not be done would be unwise and practically impossible**. As to details and methods of conducting such authorized business, involving exercise of special knowledge, and business judgment, there must be many implied powers. A strict, illiberal, or narrow construction which might hamper the exercise of a reasonable discretion by the municipal authorities in such matters, because the power is given in few words, is not, with perhaps a few exceptions, the tendency of decisions in most jurisdictions. **The courts as a rule are not disposed to interfere with the management of an authorized business, conducted by the municipal authorities presumably in the interest and for the benefit of the city and its inhabitants, unless dishonesty or fraud is manifest, or the vested power with its implied discretion has been clearly exceeded or grossly abused**.

Nelson, 289 Mich at 297; 286 NW 617 (emphasis added).

Indeed, practically speaking, municipalities must be afforded the discretion to determine how best to spend their public funds and per this Court, they have long held this discretion:

> . . . [W]e do not assume that it belongs to this court or to any other to dictate to the city how it shall spend its money. **The council must use its own discretion where it will save and where it will spend; and the case must be a very clear one, and the subterfuge very plain, before that discretion can be regarded as having been exceeded** so as to show an excess of power under a pretence [sic] of keeping within it. It is not the business of courts to act as city regulators, and unless the authority of the representatives of the citizens has been exceed their action cannot be interfered with merely because it may not seem to other persons to be as wise as it might be.

See *Torrent v Muskegon*, 47 Mich 115, 117; 10 NW 132 (1881) (emphasis added). This discretion includes the ability to decide when the municipality should loan money from its general fund to its other departments and when those departments should repay the general fund.

This matter mirrors a number of other proceedings throughout the state in which plaintiffs have decided to use the Headlee Amendment and statutory law to challenge these types of transfers and the subsequent repayments despite the fact that these transactions are, at times, critical to buoying municipal functions when they underperform. Municipalities must be able to use their discretion to decide when it is best to make intrafund (or interfund) loans, transfers and reimbursements. Otherwise, municipalities will be constrained in their ability to implement the will of the people because of a handful of malcontents or self-interested parties. By entertaining lawsuits like this one – i.e., one that challenges municipal discretion in the absence of fraud or abuse – courts invite more lawsuits (and concomitant legal costs) that are grounded in mere disagreement over how to manage municipal finances and are not centered in law. Here, the law reinforces the principle that local units are best suited to govern their own financial affairs using their well-informed discretion.

Respectfully submitted,

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By: */s/ Sonal Hope Mithani*

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Dated: September 6, 2018

CERTIFICATE OF SERVICE

I hereby certify that on September 6, 2018, I presented the foregoing document to the Clerk of the Court for filing and uploading to the electronic court filing system which will send notification of such filing to all attorneys of record.

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