REVIEW OF DETROIT PUBLIC SCHOOLS DURING STATE MANAGEMENT 1999-2016

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TABLE OF CONTENTS

BACKGROUND ........................................................................................................... 1

METHODOLOGY ......................................................................................................... 1

EXECUTIVE SUMMARY ............................................................................................... 2

OVERVIEW OF DETROIT PUBLIC SCHOOLS 1999 THROUGH 2016 ....................... 3

1994 ADOPTION OF PROPOSAL A AND K-12 EDUCATION FUNDING IN MICHIGAN ................................................................. 3
Governance of DPS 1999 - 2016 ............................................................................... 3

ANALYSIS OF DPS DECISIONS AND PRACTICES 1999 THROUGH 2016 ............. 5

DPS FACILITIES AND PROPERTY DECISIONS AND PRACTICES 1999 THROUGH 2016 ........................................................... 5

Maintenance of DPS’ Facilities ................................................................................. 5
Closure of DPS’ School Buildings ........................................................................... 6
DPS’ Purchase and Sale of Real Property ................................................................. 7
Findings Regarding DPS’ Decisions and Practices Regarding Facilities and Real Property .......................................................... 8

DPS FINANCE DECISIONS AND PRACTICES 1999 THROUGH 2016 ............... 8

DPS’ UNSOLVED STRUCTURAL CHALLENGES AND OPERATIONAL DEFICITS ................................................................. 8
Converting Short-Term Debt into Long-Term Liabilities ....................................... 9
Financial Strategy of Last Resort ............................................................................ 10
Findings Regarding DPS’ Financial Decisions and Practices ............................... 11

STAFFING AND LABOR DECISIONS AND PRACTICES 1999 THROUGH 2016 ...... 12

Alignment of Labor Cost with Declining Enrollment and Revenues ................... 12
DPS’ Staffing Challenges and the Use of Substitute Teachers ............................... 12
The Termination Incentive Program ...................................................................... 13
Findings Regarding DPS’ Staffing and Labor decisions and practices 1999 through 2016 .......................................................... 13

DPS’ DECISIONS AND PRACTICES REGARDING THE MANAGEMENT OF ACADEMICS, ENROLLMENT AND STUDENT PERFORMANCE ................. 14

DPS’ Academics ....................................................................................................... 14
The Fight for Control of DPS’ Academics ............................................................. 14
The Outsourcing of DPS’ Academics .................................................................... 16
Decisions and Practices Regarding Enrollment .................................................... 16
Findings Regarding DPS’ Academic Operations and Enrollment 1999-2016 ........ 17

CONCLUSION ............................................................................................................. 18
## EXHIBIT LIST

1. The Allen Law Group, *Detroit Public Schools – Events and Governance Timeline*.
8. Arbitration Decision re: TIP Program litigation
LEGAL MEMORANDUM
Attorney-Client Privileged

To:     Jenice C. Mitchell Ford, General Counsel
        Detroit Public Schools Community District

From:   George K. Pitchford, Esq.
        The Allen Law Group, PC

Date:   November 8, 2019

Re:      Review of Detroit Public Schools During State Management 1999-2016

BACKGROUND

Detroit Public Schools Community District (“DPSCD”) has requested that the Allen Law
Group, PC (“ALG” or the “Firm”) research and analyze Detroit Public Schools’ (“DPS”) decisions
and practices from 1999 to 2016 (the “Subject Period”) in the following areas:

1. Management of Real Property and Facilities
2. Finances
3. Staffing and Labor
4. Management of Academics and Enrollment

Accordingly, this Memorandum and its attached exhibits serve as a response to this request.¹

METHODOLOGY

This Memorandum and the information presented herein is based on research and
information gathered from several different sources. This includes in-person formal and informal
interviews with current and former staff members who have knowledge regarding DPS’ operations
during the Subject Period. In order to encourage candid discussion about sensitive issues,
interviewees were assured they would be able to maintain some level of anonymity. Therefore,
throughout this Memorandum all comments from interviewees are attributed to “Interviewees.”²
Additionally, ALG conducted a review of publicly available documents, academic writings, public
records, newspaper accounts, board meeting minutes, DPS Comprehensive Annual Financial
Reports, research papers, and historical documents provided by DPS.

¹ Please note that this Memorandum covers over fifteen (15) years of district operations. As such it is not intended to
be a complete record of the Subject Period, but instead a summary utilizing examples and significant events to explain
and provide context to the decision making and practices of DPS at that time.
² Please note that none of the interviewees were under oath when interviewed. Please further note that “Interviewees”
is a generic identification of comments and information provided by interviewees and may not always necessarily
indicate that the information was provided by more than one interviewee.
EXECUTIVE SUMMARY

An examination of the State of Michigan’s oversight of DPS during the Subject Period reveals the startling mismanagement of what was formerly one of the nation’s largest urban school districts. These missteps include the purchase of overpriced real estate without proper due diligence, inattention to aging building maintenance, and the failure to address DPS’ plummeting student achievement and enrollment. Perhaps most surprising is that the cadre of state-appointed leaders failed to even accomplish their purported primary task of addressing DPS’ fiscal challenges. Instead of taking advantage of their relative isolation from the political pressures that supposedly hindered the ability of previous elected school boards, state-appointed leaders seemingly failed to make the hard decisions necessary to right size DPS in a responsible and transparent fashion. Under state-appointed leadership, DPS engaged in questionable financial tactics and implemented temporary fixes, which allowed its debt to grow and ultimately led to the decline of DPS as it existed during the Subject Period.

In light of all of this, it is difficult to completely quantify the damage done to DPS and the community during the Subject Period. This notwithstanding, some illustrative costs worth noting include:

<table>
<thead>
<tr>
<th>Description</th>
<th>Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>Projected cost of capital repairs/renovations to DPS’ buildings that fell into disrepair during the Subject Period</td>
<td>$500 Million</td>
</tr>
<tr>
<td>Purchase of the Fisher condominium interest</td>
<td>$24 Million</td>
</tr>
<tr>
<td>Additional interest as a result of the 2011 conversion of short-term debt into long-term debt</td>
<td>$66 Million</td>
</tr>
<tr>
<td>Identified real estate overspending</td>
<td>$14 Million</td>
</tr>
<tr>
<td>Overbilling and/or improper charges by facilities contractors</td>
<td>$6 Million</td>
</tr>
<tr>
<td><strong>Total:</strong></td>
<td><strong>$610 Million</strong></td>
</tr>
</tbody>
</table>

As startling as the aforementioned information regarding the costs incurred during the state’s oversight during the Subject Period is, it likely fails to capture the most significant losses to DPS: countless students throughout the City of Detroit who were likely not afforded the educational opportunities they needed and deserved. Unfortunately, unlike some of the other losses discussed in this Memorandum, the community will likely feel the impact of these damages for generations to come, as these same students are required to enter a rapidly evolving global economy where an adequate K-12 education is a necessity.
OVERVIEW OF DETROIT PUBLIC SCHOOLS 1999 THROUGH 2016

I. 1994 Adoption of Proposal A and K-12 Education Funding in Michigan

In March 1994, Michigan voters adopted Proposal A, which fundamentally changed how K-12 schools are funded in the State of Michigan. Under the newly adopted Proposal A, schools were no longer funded by taxes on property located within the school district. Instead, a state sales tax became the primary source of school funding. Proposal A also enacted a per pupil funding formula that based a school district’s revenues on its student enrollment. This was designed to create a more equitable funding mechanism for Michigan’s schools and eliminate disparities between high property value school districts and those with a lower property tax base. Its stated goal of equality notwithstanding, Proposal A failed to truly level the playing field between the state’s districts in wealthy communities and financially struggling urban and rural community school districts. For instance, due to Proposal A’s hold harmless exception, Birmingham Public Schools received $11,924 per student in state aid during the 2015-16 school year, while Detroit Public Schools only received $7,434 per student in state aid. In addition to overhauling how Michigan’s school districts were funded, Proposal A also allowed for funding dollars to easily follow students from one school district to another. This opened the door for schools of choice, encouraging school districts to enroll students from outside their districts and compete with one another for students. Additionally, the portability of education funding built into Proposal A would also serve as a springboard for the expansion of charter schools, especially in urban cities such as Detroit.

II. Governance of DPS 1999 - 2016

During the Subject Period, DPS’ persistent financial challenges set the stage for a series of state takeovers. The state’s first foray into running DPS was packaged as a mayoral takeover. Under Public Act 10 of 1999 (“PA 10”), the governance powers of DPS’ elected school board were suspended and its members were deemed ineligible for appointment to the newly formed school reform board (the “Reform Board”), to which the Mayor of the City of Detroit was required to appoint six (6) out of seven (7) members. Also, pursuant to PA 10, the seventh member of the Reform Board was the state’s Superintendent of Public Instruction or their designee. A state level appointee being given a voting position on the Reform Board is notable because under Section 374(1) of PA 10, DPS’ Chief Executive Officer (“CEO”) had to be selected by unanimous vote. This represented one of the first times the state directly inserted itself into the governance of DPS

3 See Exhibit 1, Detroit Public Schools – Events and Governance Timeline.
5 Despite the stated intent to encourage a more equitable distribution of education funding, Proposal A’s Per Pupil Allowance Formula does not consider student specific needs that may also impact funding needs. Moreover, under Proposal A, many of the school districts that previously benefitted from higher funding because of their higher property tax base were deemed “hold harmless” school districts and continued to receive funding in addition to the per pupil allocation.
6 Exhibit 2 at Sec. 372(2)(b).
7 Id. at Sec. 374(1).
by granting a state representative voting privileges on the Reform Board and retaining the authority to exercise a *de facto* veto over other members regarding the selection of the CEO. Moreover, although selected and not elected, the CEO would essentially have the powers traditionally associated with both an elected board and a superintendent.

The Reform Board and the CEO governed DPS for five (5) years. In what would become an unfortunate pattern, the exodus of students out of DPS actually increased during this time. Consequently, at the end of the Reform Board and CEO’s five (5) year terms, they managed to turn a surplus left by the former elected board into a significant deficit. In 2005, in accordance with PA 10, DPS’ electorate got to decide whether it wanted DPS to keep the Reform Board and CEO, and voted to return DPS back to an elected school board.

In 2009, after just three (3) years of control by an elected school board and with a deficit of over $400 million, the state declared a financial emergency and appointed DPS’ first Emergency Manager pursuant to Public Act 72 of 1990 (“PA 72”). Although the elected board members remained in office, they were considered powerless with regards to DPS’ finances and operations. Moreover, under PA 72, the state directly intervened in the governance of DPS and took over the district. The new Emergency Manager was granted even broader authority than the CEO under the Reform Board. Despite these efforts by the state, DPS continued to lose students and funding at an alarming rate. In an unfortunate continuation of the pattern set by the Emergency Manager’s CEO predecessor, three (3) years after his appointment and despite significant cuts to expenditures, DPS still had a deficit in excess of $283 million. This pattern would continue for the next seven (7) years as different Emergency Managers attempted and ultimately failed to salvage DPS’ finances.

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8 Exhibit 2 at Sec. 374(4).
9 Id.
10 Exhibit 3 at 84.
11 Karla Socon Reid, “Detroit’s First Elected Board in 6 Years to Face Challenges,” *Education Week*, November 8, 2005.
12 Public Act 72 of 1990 refers to the title Emergency Financial Manager. In 2011, Public Act 4 of 2011, a successor statute to Public Act 72 of 1990 was adopted and changed the title to Emergency Manager. This successor statute was short lived, however, as it was repealed in a statewide voter referendum in late 2012. Governor Snyder and the legislature quickly responded to this and adopted Public Act 436 of 2012 that same year, which was similar to the repealed Public Act 4 of 2011 and retained the new title of Emergency Manager, but contained additional language so that voters could not repeal it by way of a referendum. Accordingly, for the sake of clarity, all individuals appointed under any of these laws are referred to as Emergency Managers throughout this Memorandum. See “Detroit School Charade Stalls Financial Reformer,” *The Detroit News*, Dec. 12, 2008.
13 See MCL 141.1201 *et. seq.*
14 Exhibit 4 at 125.
I. DPS FACILITIES AND PROPERTY DECISIONS AND PRACTICES 1999 THROUGH 2016

a. Maintenance of DPS’ Facilities

Throughout the Subject Period, there were significant issues with building maintenance throughout DPS. DPS’ teachers and staff routinely complained about deplorable building conditions. In August 2016, DPS’ teachers staged a series of sick-outs in protest of the dilapidated building conditions and forced 88 of DPS’ schools to shut down.15 That same year, prompted by the complaints, the Mayor of the City of Detroit took a personal tour of four (4) of DPS’ buildings, and based on that tour, ordered inspections of all DPS’ buildings.16 During these inspections, inspectors found over 150 violations of health and building codes.17 Some of the more egregious violations included insects and rodents in buildings, signs of water damage in the ceilings, and mold/mildew found growing in at least two (2) classrooms.18 Already facing various financial challenges, DPS was forced to divert precious capital from other priorities in order to immediately remedy the violations to the City of Detroit’s satisfaction.

In addition to what was uncovered by employees’ complaints and the City of Detroit’s inspections, a 2018 independent facilities assessment conducted by OHM Advisors further confirmed that DPS’ facilities had been allowed to fall into disrepair during the Subject Period. According to OHM Advisors’ report, approximately 25 of the 52 district buildings assessed were rated as being in poor or unsatisfactory condition.19 Moreover, OHM Advisors estimate the cost of completing the necessary capital repairs and upgrades to be in excess of $500 million, and project that this cost will grow to over $1.5 billion over the next ten (10) years.20

Interviewees provided mixed feedback when asked about DPS’ decisions and practices regarding building maintenance during the Subject Period. They noted that DPS was able to modify and/or eliminate onerous collective bargaining provisions and agreements with various maintenance unions that were inefficient and financially unsustainable. Additionally, under the Emergency Manager, DPS outsourced building maintenance to third-party contractors, which interviewees acknowledged resulted in significant savings. However, Interviewees expressed concern about the effectiveness of some of the contractors. They noted that at least one (1) of the former contractors would routinely cut corners and under staff the buildings, leaving them in unacceptable conditions. Additionally, contractors failed to complete routine maintenance on the buildings’ various systems, which would often lead to unnecessary costs incurred by DPS. Moreover, according to confidential information, one contractor had overbilled, charged for inappropriate expenses, and/or unauthorized expenses overcharged DPS for skilled tradesmen.

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15 Ann Zaniewski, “Judge Rules Against DPS in Teacher Sick-Out Case,” Detroit Free Press, Aug. 18, 2016. It should be noted that many of the teachers that participated in the sick-outs also stated concerns about low wages and other conditions.
17 Id.
18 Id.
19 Exhibit 5 at 18-21.
20 Id. at 26.
tools and services in excess of $5,500,000. Interviewees noted that these concerns were brought to the CEO’s and various Emergency Managers in control of DPS during the Subject Period but felt that they were ignored in favor of more “pressing concerns.” These events, all occurring during the Subject Period, were apparently a result of a lack of appropriate oversight and unchecked spending.21

b. Closure of DPS’ School Buildings

The results of a review of DPS’ facilities decisions and practices regarding the closure of school buildings during the Subject Period are startling.22 In 2000, approximately 288 school buildings were open; by 2015, only 93 remained open.23 During the Subject Period, DPS was responsible for shuttering over 175 buildings and ensuring that these assets were properly protected and maintained. Unfortunately, based on available data, properly closing and protecting the vacant buildings was not a priority for DPS’ various leadership teams. In 2015, a local non-profit organization conducted an independent survey of the approximately 81 vacant buildings. According to the published results of its survey, only 37 of the buildings were properly secured, 45 had simply been abandoned and were accessible to trespassers and vandals, and 26 were completely exposed not only to trespass and vandalism, but also the elements.24 The report also noted that all of the buildings, secured or otherwise, had suffered damage from scrappers and/or fire.25

Information provided by Interviewees supports the findings of the independent study regarding the condition of DPS’ vacant buildings. Interviewees stated that during the Subject Period, Emergency Managers failed to allocate the funds sufficient to properly close the buildings. Interviewees recounted stories of employees from various departments showing up on the weekends with their own tools and supplies to try their best to better secure the buildings on their own. Interviewees reiterated that proper closure of the buildings and thus preservation of these assets either was not a priority, or DPS did not have adequate funds to keep up and complete the projects properly. Interviewees noted that these challenges were only exacerbated by a lack of coordination between DPS and the Detroit Police Department. It became common knowledge in the community that DPS’ closed buildings were poorly protected and therefore easy targets for scrappers and vandals. As DPS lurched from one financial crisis to another during the Subject Period, this lack of strategic planning and effective prioritization was seemingly typical of DPS’ state-appointed leadership. Moreover, it appears that there was an issue of bandwidth, as closures were often done so haphazardly that the meager resources DPS had allocated to the effort would quickly become overwhelmed, forcing employees to make difficult decisions about what would and would not get done.

21 The cites and references to the confidential information referenced and relied upon on this section have been intentionally omitted.
22 Exhibit 6.
24 Id.
25 Id. at 42-45.
Regardless of the cause, the failure of state-appointed leadership to properly address this matter may have resulted in many of these vacant buildings becoming blight in their Detroit communities, or even worse, safety hazards. Additionally, as they continue to deteriorate, any remaining potential value as real estate may be lost, costing DPS a much-needed alternative source of potential revenue.

c. DPS' Purchase and Sale of Real Property

Many of the decisions during the Subject Period regarding the sale and purchase of real property are troubling. For instance, the 2002 purchase of the condominium interest in the Fisher Building for over $24 million as part of the 1994 Capital Improvement Bond Program was fraught with issues, giving rise to concerns of overpayment, conflicts of interest, and poor judgment. According to reports, DPS’ state-appointed CEO decided to purchase the Fisher Building space to serve as DPS’ new administrative headquarters. The structure of this transaction was described as “non-traditional” from the start. If nothing else, it was unusual and troubling to some of the staff members working on the matter that the seller was also serving as DPS’ broker. Moreover, citing the unique nature of the transaction, DPS’ leadership decided to move forward with the purchase without receiving a formal evaluation or appraisal of the potential market value of the condominium interest they were buying on behalf of DPS. Although no post-purchase due diligence was ever completed to confirm whether DPS had spent too much on the space, DPS’ own attorney for the transaction described the purchase as “grossly overpriced” and attempted to renegotiate some of the terms. DPS’ former broker flatly refused, and only offered to purchase some of the space back at a price far less than what they had just sold it to DPS.

These issues continued to arise even after the purchase of the Fisher Building space was completed. Although $4 million of the sale price had been allocated for buildout costs, after the purchase was complete it was realized that the actual cost of the buildout would be in excess of $18 million. In spite of the fact that this buildout was no longer simply preparing the space for DPS, the decision was made to proceed with the project and select contractors to complete the work without even going through a competitive bid process. Moreover, even though the original allocation was originally intended to fund the entire purchase and buildout with bond dollars, because the nature and scope of the buildout project had changed so drastically, DPS was ultimately forced to spend $5 million from its own general fund to complete it, despite millions of bond dollars still being available. Leadership failed to appropriate the funds needed to prepare the space for DPS’ use, which further exacerbated DPS’ financial deficit.

Reform Board members at the time of the purchase also confirmed they had little to no say in these matters and expressed general frustration at how powerless they were in their advisory role to the CEO. A member of the Reform Board may have best summed up the concerns about the transaction when he recalled that he did not understand how it helped DPS to sell its ownership of one old building to buy a condominium interest in another old building.

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26 Cites have been omitted from this section, as the sources referenced are confidential.

27 The cites and references to the confidential sources relied on in this section have been intentionally omitted. The report can be requested from the DPS Office of the General Counsel.
d. Findings Regarding DPS’ Decisions and Practices Regarding Facilities and Real Property

Plagued by mounting financial woes during the Subject Period, DPS seemingly employed a haphazard approach to maintaining its facilities. Moreover, building closures were given a low priority and likely suffered from both a lack of funding and direction. This appears to have been a costly mistake, as many of the vacant buildings have been stripped and/or vandalized. These decisions and the failure to engage in strategic decision making undoubtedly had a lasting negative impact on DPS. Moreover, it represents yet another instance of how the current leadership must bear the burden of previous state-appointed leadership’s decisions.

It would be difficult to conduct a review of every real estate transaction during the Subject Period, but if the murky purchase and improvement of the condominium interest in the Fisher Building was in any way typical of DPS’ approach to the sale and/or purchase of real estate, then there is cause for grave concern. That transaction demonstrated a surprising disregard of fairly common best practices, such as obtaining an appraisal prior to purchasing real estate. Moreover, even some of the employees working on the transaction felt that DPS paid far too much for the property, which gives rise to the concern whether DPS was routinely paying too much in real estate transactions during the Subject Period, and whether transactions were free of any conflicts of interest.


a. DPS’ Unsolved Structural Challenges and Operational Deficits

When considering DPS’ decisions and practices regarding finances during the Subject Period, it is necessary to remember that DPS, like many other districts, had been chronically underfunded since the adoption of Proposal A. Despite this reality, during the Subject Period, DPS’ leadership either refused or failed to address the challenges this fact presented. As such, DPS consistently spent significantly more money than it brought in as revenue, which led to operational deficits that needed to be addressed by some combination of reducing expenditures, and increasing revenue, or at the very least reducing the rate at which revenues were falling. During the Subject Period, the state’s Emergency Managers failed to take any of these actions while DPS’ operational deficits continued to skyrocket. For instance, in FY 2006 DPS had a small but positive fund balance of 20.6 million. By FY 2011, just five (5) years later, the unchecked spending resulted in an operational deficit of $284 million.

In the opinion of Interviewees with knowledge about the decision making during the Subject Period, the failure to address DPS’ structural financial issues came down to an unwillingness of the leadership to “make hard decisions.” As an example, Interviewees pointed to DPS’ failure to align building utilization to the actual student populations. According to Interviewees at various points during the Subject Period, it was not uncommon for district buildings with the capacity for thousands of students to have less than three hundred (300) students in them. Even worse yet, newly built buildings would sometimes go underutilized, while costlier

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29 Exhibit 4.
and less efficient older buildings in the same vicinity would also remain open and underutilized. With factors such as these draining DPS’ resources, Interviewees felt that it was clear to DPS’ CEO and Emergency Managers that building usage needed to be strategically realigned with the shifting population trends in the City of Detroit. Nevertheless, Interviewees recalled witnessing these issues be ignored until they reached crisis level proportions. When finally addressed, the issues would be dealt with in an inefficient and reckless manner, with little thought to the overall strategy and direction of DPS, and ultimately costing DPS rather than having a positive effect on its finances. The only explanation Interviewees could offer for the repeated failures of the state-appointed leadership to proactively seize the initiative on these tough issues was politics and fear, as many of the unelected state-appointed leaders either did not have a mandate or the trust of the community and were therefore hesitant to take on controversial issues such as school closings, until they had no choice.

Although these are Interviewees’ personal perspectives, there is evidence to support their assertions, such as the failure to adequately respond to DPS’ growing operational deficits. This is troubling, as one of the stated purposes of utilizing state appointed leaders such as Emergency Managers is that they are insulated from politics and able to make tough financial and operational decisions in the best interest of DPS and its students. Based on the available data and the Interviewees’ assessment, however, it appears as if the opposite may have been true. Installed by the state, and therefore lacking any connection and/or trust from the community, coupled with the sensitivity surrounding the issue of state control of DPS, it appears that the state-appointed leaders may have felt they lacked the support to take on some of the structural issues plaguing DPS and its finances.

b. Converting Short-Term Debt into Long-Term Liabilities

In addition to its general obligation debt for which the responsibility falls directly on the taxpayer, DPS also issues short-term notes, often referred to as State Aid Notes, to address its challenges with cash flow. Unlike the general obligation debt, this obligation is serviced directly from DPS’ general fund and is secured by DPS’ state aid funding. As such school districts normally repay these debts out of their general fund in the same year they are issued.

Faced with mounting operational deficits and instead of addressing the underlying structural issues, DPS converted this short-term debt into a long-term liability on several occasions during the Subject Period. This strategy allowed DPS to treat short-term loans to address cash flow issues as additional revenue and gave the appearance of progress with respect to DPS’ financial challenges. In 2005, while under the control of the CEO and Reform Board, DPS converted a $210 million cash flow borrowing into a long-term liability to be repaid over 15 years and further artificially delayed its latest financial crisis by not requiring repayment of the debt to start until 2007.30 This also forced DPS to pay for these liabilities out of future general funds and take on more debt in the form of increased interest payments. Additionally, because these dollars could now be treated as revenue, it also gave the appearance that DPS had somehow balanced the

In reality, this effectively diverted future dollars that should be used in the classroom, and at best DPS’ leadership only delayed the inevitable shortfall to a later date. Predictably, just five (5) years after repayment on the original debt was supposed to have commenced, DPS still owed $141 million of the original $210 million debt. Now under the control of an Emergency Manager, the state allowed DPS to refinance this debt yet again and stretch the payment schedule out until June 2020. Once again, this resulted in DPS having to pay more in interest, and yet another pledge of future dollars originally intended for the classroom.

This would not be the last time DPS used this questionable strategy to avert a fiscal crisis. In October 2011, DPS borrowed $420 million to help with its cash flow. As DPS’ revenues continued to fall, the Emergency Manager received authorization from the state to convert $231 million of the original borrowing into a long-term ten (10) year liability. This was at an additional interest cost of approximately $66 million, with an annual debt service from DPS’ general fund of $32 million over the ten (10) year life of the liability. Additionally, since the conversion to a long-term liability allowed the borrowing to now be treated as revenue for the general fund, it again gave the false appearance that DPS’ operating deficit at the end of FY 2011 had been reduced from $284 million to $83 million at the end of FY 2012.

The impact of these conversions of DPS’ short-term debts into long-term liabilities was significant. By June of 2014, DPS had incurred approximately $299 million in long-term liabilities as a result of converting and then refinancing what were originally supposed to be short-term cash flow borrowings. The cost of servicing this debt was over $52 million dollars per school year, most of which had to be paid out of DPS’ general fund. That amounted to a total cost of approximately $1,100 per pupil diverted from DPS’ $7,552 per-pupil foundation allowance each school year to debts as old as ten (10) years. It is difficult to assess whether this conversion technique was the appropriate response to DPS’ financial challenges during the Subject Period. This notwithstanding, it is undeniable that it created a real risk of forging a false sense of security for DPS and its officials, as operational deficits were artificially lowered, and the structural financial crisis could continue to go unaddressed. Moreover, it is worth also noting that conversion of short-term cash flow debt into a long-term liability is not a common practice for Michigan school districts.

c. Financial Strategy of Last Resort

Dubious borrowings and conversions of debt were not DPS’ only coping mechanism with its financial challenges during the Subject Period. Faced with both revenue and cash flow challenges, during truly desperate times DPS would simply not pay some of its financial obligations. Interviewees recalled this unconventional approach to finances and cash flow management taking various forms. Sometimes DPS would simply not pay for its utilities based on

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31 Id. at 4-5.
32 Id.
33 Id.
34 Id.
35 Id.
36 Id. at 4.
the assumption that the City of Detroit and other utilities would not be willing to shut them off, and other times various vendors and district partners would have to go months without having their invoices settled.

In FY 2015, while DPS was under the authority of an Emergency Manager, this non-payment strategy was expanded in a troubling fashion. Despite state law requiring all Michigan school districts to make monthly contributions to the Michigan Public School Employees Retirement System (“MPSERS”), the multi-employer cost-sharing retirement plan for public school employees run by the State of Michigan, DPS consistently failed to make the payment. Unlike previous implementations of this strategy, this instance resulted in a significant debt of $80 million owed to the State of Michigan. The situation became so serious that MPSERS threatened to garnish DPS’ state aid payments in order to settle the debt. Had MPSERS moved forward with this threat, it likely would have resulted in the collapse of DPS. Moreover, it is noteworthy that a portion of the funds that DPS was withholding from MPSERS were required contributions from DPS’ own employees. Therefore, for a period of time, it is highly likely that DPS was not only operating on its employees’ money, but maybe even paying them at least in part with their own money. Again, as with the aforementioned short-term loan conversions, it is unclear what the ultimate strategy was behind DPS withholding tens of millions of dollars from the state’s retirement fund in violation of the law. It may have been some sort of attempt to negotiate with the State of Michigan regarding DPS’ financial obligations, or perhaps it was the last resort when it became clear that there were insufficient funds to operate DPS.

d. Findings Regarding DPS’ Financial Decisions and Practices

During the Subject Period, DPS failed to address DPS’ structural financial issues. Expenditures continued to exceed dwindling revenues, which led to expanding operational deficits each school year. This may have been due in part to the reluctance of DPS’ leadership to make tough and potentially unpopular decisions. Moreover, even when forced by DPS’ fiscal woes to make such decisions, they were done haphazardly and sometimes did more harm to DPS than good. As a result, DPS engaged in questionable borrowing that resulted in significant debts. Moreover, DPS implemented a risky strategy of not paying its obligations, sometime in violation of the law, that seemed to accomplish little other than to allow DPS to limp towards the next inevitable fiscal crisis.

III. STAFFING AND LABOR DECISIONS AND PRACTICES 1999 THROUGH 2016

a. Alignment of Labor Cost with Declining Enrollment and Revenues

Historically, a significant contributing factor to DPS’ financial and operational woes was labor costs. These challenges were driven by costs related to salaries, benefits, and inefficient work rules. The data from DPS during the Subject Period, however, demonstrates that DPS made significant gains in aligning its labor cost with the shrinking student population. In 2005, DPS had over eight thousand (8,000) teachers. By 2015, however, that number had dropped to three

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39 Exhibit 7 at 7.
thousand (3,000), representing a 62.5% reduction in just ten (10) years.\textsuperscript{40} During that same period, the number of DPS’ administrators went from 583 to 333, which represents a 42.9% reduction.\textsuperscript{41} Although not necessarily determinative, this was at least proportionate to the enrollment trends during that same period, which went from 141,000 students in 2005 to 47,280 students in 2015, representing a 66.5% drop.\textsuperscript{42} Therefore, unlike many other areas of DPS, such as finances and facilities, DPS’ staffing levels in two of the largest labor pools, administration and teachers, kept pace with declining student enrollment.

During the Subject Period, it appears DPS also kept salaries aligned with DPS’ shrinking enrollment and revenue. According to the available data, in 2015-2016, the state average for public school teachers’ salaries was $61,875.\textsuperscript{43} DPS teachers at that same time were only making an average of $63,716, a difference of less than $2,000. This parity in pay was at least in part due to the various concessions that DPS’ teachers agreed to or were otherwise imposed upon them. No definitive records of the concessions were available, however, according to Interviewees. Starting in 2005, various groups around DPS, including the teachers, agreed to a variety of concessions including a 5% wage reduction and furlough days. Interviewees also noted that despite recent efforts to achieve some parity in compensation, some of the teachers that took these 2005 concessions still have not returned to their 2005 pay levels, fourteen (14) years later.

b. DPS’ Staffing Challenges and the Use of Substitute Teachers

Based on the alignment between the staffing levels and enrollment during the Subject Period, it is arguable that the CEO and particularly the Emergency Managers effectively managed DPS’ staffing levels and related costs through concessions and layoffs. It is important, however, to understand whether this was accomplished without adversely impacting DPS’ classroom environment. According to Interviewees, it was not. In addition to reportedly devastating the morale of DPS teachers with these reductions and concessions, Interviewees asserted that during much of the Subject Period, it became clear that a major part of the Emergency Manager’s financial and staffing strategy was to maximize the utilization of substitutes instead of full-time teachers in order to realize a significant savings. Interviewees reported at any given time there could be more than five hundred (500) active substitutes teaching children in DPS, with little to no effort to find full-time teachers to replace them. Interviewees also recounted how the use of substitutes became so pervasive during the Subject Period that there were some substitutes that taught a class for an entire school year akin to a full-time teacher. Interviewees noted that they openly worried about whether DPS’ children were getting the best educational opportunities with so many substitutes taking the place of full-time certified teachers throughout DPS, but leadership ignored these concerns, or dismissed them with the excuse that DPS was unable to recruit qualified teachers because of the reduced pay and benefits DPS’ teachers received. This was somewhat ironic in light of the fact that often times it was the very same state-appointed officials who had negotiated and/or imposed these labor concessions that now apparently made it difficult to recruit and retain enough full-time educators.

\textsuperscript{40} Id.
\textsuperscript{41} Id.
\textsuperscript{42} Exhibit 7 at 6.
c. The Termination Incentive Program

The rampant use of substitute teachers was not the only attempt during the Subject Period to extract savings out of DPS’ staff. In 2009, DPS’ Emergency Manager implemented a new initiative with the hopes of relieving some of the pressure from DPS’ cash flow. The program was called the Termination Incentive Plan (the “TIP Program”) and was negotiated into DPS’ collective bargaining agreements. Under the TIP Program, beginning in January 2010 and ending in December 2012, affected employees had $250 deducted from each paycheck, and the funds were deposited into a “TIP Account,” where they would be held until an employee separated from DPS. Upon separation, the employee would be eligible for a $1,000 bonus for each year of service (up to 9 years of service). In other words, DPS created a new post-employment benefit at its own expense and had once again converted a short-term debt obligation, a portion of employees’ salary, into a long-term liability. While the TIP Program was in place, DPS collected millions from employees with the promise that they would recoup the funds upon their separation from DPS.

Once again demonstrating a lack of continuity in strategy between the various Emergency Managers during the Subject Period, a new Emergency Manager was appointed and promptly terminated the program prior to its originally agreed upon December 2012 end date and refused to payout some of the employees per the terms of the program when they left DPS. The teacher’s union objected to DPS seemingly breaking its promise to its members and filed a grievance on the matter, which was arbitrated. As a further indicator of just how little continuity there was amongst the Emergency Managers, Interviewees confirmed that the prior Emergency Manager showed up the day of the hearing and testified on behalf of the teachers’ union and against the newly appointed Emergency Manager. DPS unsurprisingly lost the arbitration, costing the district millions in backpay.


The Interviewees’ observation regarding DPS’ staffing and labor decisions and practices were particularly insightful. When asked for their reflections on how staffing and labor issues were dealt with during the Subject Period under the CEO and various Emergency Managers, the Interviewees immediately stated that they appreciated the flexibility provided by the Emergency Managers’ broad authority in these matters but were deeply troubled by the lack of accountability regarding how they used that authority. To the Interviewees’ point, under every incarnation of the Emergency Manager laws, the state-appointed Emergency Managers possessed an incredible amount of authority over staffing and labor matters such as collective bargaining agreements. It appears that they were able to leverage that authority to effectively address some longstanding issues, such as staffing levels and ensure they remained proportionate to student enrollment, while also seemingly controlling wages by negotiating and/or implementing various cost-saving concessions. On the other hand, these issues were addressed with very little oversight and/or accountability. As a result, countless students were educated by substitutes, who may not have been certified in the subject matter they were teaching, for as long as an entire school year. Additionally, DPS once again engaged in the shuffling of employees’ funds and the creation of additional long-term debt, and then the premature termination of a program it had negotiated with

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44 Exhibit 8.
the union. Therefore, the impact on DPS and its students of some of these decisions may never truly be known or entirely quantifiable.

IV. DPS’ DECISIONS AND PRACTICES REGARDING THE MANAGEMENT OF ACADEMICS, ENROLLMENT AND STUDENT PERFORMANCE

a. DPS’ Academics

Despite some initial gains that were quickly erased while the Reform Board and CEO ran DPS, the academics of DPS’ students suffered during the Subject Period.\(^{45}\) For example, DPS’ test scores continued to lag behind state averages in almost every category.\(^{46}\) Studies conducted by the National Assessment for Educational Progress indicate that by 2013, only 4 percent of 4th-grade students were proficient in math and only 7 percent were proficient in reading.\(^{47}\) While this was an improvement from 2009, DPS students were scoring consistently lower than the state averages by roughly 35 points in math and 30 points in reading. In fact, regarding both the 4th and 8th grade reading and math score trends, DPS was consistently lowest compared to several other major urban cities including Chicago, Milwaukee, and Cleveland.\(^{48}\) Unlike other areas reviewed, there seem to have been very few efforts to address issues such as unacceptable dropout rates, lack of teacher accountability, and system-wide funding inequities in the area of academics. Focused improvement in any of these areas may have had a significant positive impact on DPS’ academic operations and overall student achievement. Even a few of the major academic initiatives that were attempted during the Subject Period, such as the formation of the Education Achievement Authority (the “EAA”), were primarily driven by the state.\(^{49}\) It appears as if DPS’ state-appointed leadership, especially the Emergency Managers, were more focused on trying to fix DPS’ finances and may have somewhat neglected DPS’ academics. One observer who conducted a study of this issue, bluntly concluded that “[t]he data analysis revealed that there were no significant education reforms in Detroit Public Schools from 1999-2014.”\(^{50}\) A DPS teacher that he interviewed for his study echoed this sentiment, stating that “I cannot think of one impactful initiative the Detroit Public Schools instituted from 1999–2014 on a district level.”\(^{51}\) This laissez-faire approach towards DPS’ academics resulted in a school district that failed to implement any significant district-wide best educational practices for almost two (2) decades, which reduced its ability to recruit and retain students. Once again, it is hard to calculate the impact of this potential failure as countless students may have been deprived of important educational opportunities and left unprepared to move forward with their education and/or careers.

b. The Fight for Control of DPS’ Academics

The lack of initiative regarding DPS’ academic operation is made even more puzzling by the fact that DPS’ Emergency Manager, Governor Snyder, and the state’s legislature went to great

\(^{45}\) Exhibit 12.

\(^{46}\) Id.

\(^{47}\) Id.

\(^{48}\) Id.


\(^{51}\) Id.
lengths to assert their collective authority over DPS’ academics. In 2009, after the appointment of DPS’ first Emergency Manager pursuant to Public Act 72 of 1990 (“PA 72”), the elected board still retained their offices, but were considered powerless and largely ignored by the new Emergency Manager. In 2011, DPS was facing yet another financial crisis in the form of a potential operational deficit of hundreds of millions of dollars. Without meeting or having any discussions with the elected school board, the Emergency Manager announced that he would be shutting down nearly half of DPS’ schools, conducting massive layoffs of teachers and staff, and drastically increasing class sizes throughout DPS.

The elected board felt strongly that the Emergency Manager’s proposed sweeping reductions had exceeded the scope of his authority under PA 72 and responded by filing for an injunction to halt his plans to shutter half of DPS. In its filings, the elected board claimed that the Emergency Manager’s reductions were so drastic that they would materially impact the academics and learning environment of DPS, which the Emergency Manager did not have the authority to do, as PA 72 only gave him authority over DPS’ finances. The judge in the matter agreed with the board and granted its request for an injunction. In February 2011 the judge held that Emergency Managers’ powers were not all encompassing and ordered DPS’ Emergency Manager to cede academic control back to the elected board, as well as to cease interference with the board and its duties.\(^{52}\)

Despite a seeming reluctance of the Emergency Manager to address DPS’ academic operations and programs, this was now deemed a high priority by not only the Emergency Manager, but also his supporters in Lansing. In March 2011, less than sixty (60) days after the judge’s ruling granting the elected board authority over DPS’ academics, Governor Snyder and the Michigan legislature repealed PA 72, which DPS’ Emergency Manager had been appointed under, and replaced it with Public Act 4 of 2011 (“PA 4”), which expressly gave Emergency Managers in school districts authority over academics.\(^{53}\) This new law did not last long, however, as PA 4 was repealed by statewide voter referendum in 2012. This issue was so important, however, that less than thirty (30) days after voters had struck down PA 4, the Michigan legislature passed another version of the legislation, making sure to clarify that Emergency Managers in school districts had authority over academics. Language regarding appropriations was added to the legislation, which made this version immune from another voter referendum.\(^{54}\)

It was apparently important to the Emergency Manager and his allies in Lansing that he and any subsequent Emergency Managers have sole authority over DPS’ academic operations and programs. This arguably creates a certain responsibility on the part of the Emergency Manager as well as the State of Michigan regarding DPS’ students’ academic performance during the Subject Period and begs the question of what any of the Emergency Managers did regarding DPS’ academics and the impact on student performance.

\(^{52}\) Exhibit 9.
\(^{53}\) Exhibit 10 at Sec. 17(1).
\(^{54}\) Exhibit 11.
c. The Outsourcing of DPS’ Academics

As stated above, DPS’ Emergency Managers tended to focus on DPS’ finances and operations. This resulted in a certain amount of neglect of DPS’ academic operations and programs throughout the Subject Period. A notable exception occurred in July 2009, when early in his tenure and armed with $20 million in one-time Title I federal stimulus money, the Emergency Manager made a proposal to fundamentally alter how DPS was providing instructional services at the high school level. His proposed solution demonstrated how he and most likely his successor Emergency Managers viewed their role regarding DPS’ academics. In short, he proposed engaging four (4) educational management companies to “assist” with running the day-to-day operations of seventeen (17) of DPS’ twenty-two (22) remaining high schools.55 Provided with both the funds and authority necessary to directly have a meaningful impact on DPS’ academic operation and student achievement, he opted to instead outsource the task to an outside third party. Moreover, it did not go unnoticed that the Emergency Manager had proposed the same operational model used by many charter schools, who often utilize third-party companies to manage the day-to-day operations of their schools. Therefore, despite the legal and political struggles to establish the Emergency Manager’s authority over the academics of DPS, he did not demonstrate a genuine desire to be directly engaged in DPS’ most critical function.56

d. Decisions and Practices Regarding Enrollment

During the Subject Period, some of the factors that significantly influenced DPS’ declining enrollment were beyond the control of anyone at DPS. For instance, the U.S. Census Bureau estimates that in 1999 the population of the City of Detroit was just over 975,000, however, by 2016 the population had dropped to 672,795. The city had lost nearly one third of its population in less than two (2) decades, which would inevitably lead to a smaller student population.57 Also, of particular import to a community school district, the entire State of Michigan experienced a noticeable and continuing drop in its birth rate just prior to and during the Subject Period. From 1989 to 2016, Wayne County experienced a 41% reduction in the number of births each year. As a result, in addition to there being less people in the City of Detroit, even those that still lived there were having less children, which further reduced the potential student population.58 Both of these are factors out of the control of DPS’ leadership that may have had a significant impact on DPS’ ability to attract and retain students during the Subject Period.

Although the aforementioned factors may have been out of the control of DPS’ state-appointed leadership, many other important factors could have been addressed. First, the

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55 The four educational management companies hired were: Edison Learning, Institute of Student Achievement, EdWorks and Model Secondary Schools Project.
56 It should be noted that the Emergency Manager’s plan for the management of DPS’ high schools coupled with his strategy of an aggressive advertising campaign failed to stop the flow of students out of DPS. Moreover, DPS projected that it would lose another 70,000 students by 2014, which would cripple DPS’ operations. Facing a mounting operational deficit and dire predictions regarding future enrollment, it was at this point the Emergency Manager proposed the plan to shutter half of DPS’ schools mentioned above.
58 Julie Mack, “Michigan Birth Rate Ties Record Low; See Numbers for Your County,” MLive, June 11, 2018.
aforementioned years with no real focus on DPS’ academic operations undoubtedly had a negative impact on enrollment, as there was little offered that would entice students and parents to come to DPS and/or remain members of its educational community. This factor became especially important after the passage of Proposal A, which was purposely designed to make it easier for students to attend the school of their choice. It was therefore somewhat predictable that in the absence of a strong academic program, DPS would continue to lose students to surrounding districts and charter schools.

Likely one of the most significant factors that led to the decline in enrollment was the rapid expansion of charter schools in the City of Detroit during the Subject Period.59 Faced with this challenge, DPS’ Emergency Managers exhibited inconsistent responses. Some Emergency Managers seemed to view the quickly multiplying charter schools as competition for much needed funding and took purposeful action to curtail further expansion of the new educational alternative in the city. Others Emergency Managers seemed to view the charter schools as potential partners in education and actually facilitated their growth by allowing them to use DPS’ facilities, even having DPS charter schools that would ultimately compete with the district. Although opinions may differ regarding which of these strategies DPS should have adopted, it is undeniable that the number of charter schools in Detroit increased exponentially during the Subject Period, and that DPS’ students and the corresponding funding flocked to these new educational opportunities.

e. Findings Regarding DPS’ Academic Operations and Enrollment 1999-2016

There was perhaps no more significant shortcoming of DPS and its leaders during the Subject Period than the failure to address DPS’ declining academics and enrollment. After Proposal A was enacted, funding became inextricably linked to enrollment, and regardless of what promises were made, there is little reason to believe that DPS would have ever made any meaningful gains in enrollment without first improving its academic programs and performance. Despite this, it appears that DPS’ academic program received little attention from Emergency Managers, who instead focused on DPS’ finances. This seeming neglect of the academic program may have accelerated the decline in enrollment, as the data demonstrates that even students who were already at DPS schools were leaving DPS for other educational opportunities.

**CONCLUSION**

Without input or consent from DPS or its electorate, for most of the time period of 1999 through 2016, the State of Michigan effectively took over the operation of DPS. Despite the intent when this takeover was first initiated, in every area reviewed, DPS is significantly worse off after state rule. District funds and assets, including its property and buildings, were squandered in questionable real estate transactions that lacked not only due diligence, but also transparency. Buildings, both occupied and unoccupied, were also allowed to waste away due to neglect or a failure to provide routine maintenance services. Also, DPS’ finances worsened significantly, as the state and its agents failed to address the structural operational issues plaguing DPS and align DPS’ expenses with its revenues. This led to larger and larger operational deficits and cash flow challenges that would eventually cripple DPS’ operation and almost drive DPS into bankruptcy. Moreover, during this entire time, the state did not successfully address DPS’ rapidly declining enrollment as parents and students, provided with no incentives to stay, poured out of DPS to competing school districts and charter schools in the City of Detroit. Instead of effectively dealing with these issues, the state’s Emergency Managers engaged in a number of borrowing and debt conversion schemes that have resulted in debts that will have to be repaid for years to come. Maybe most importantly, the state failed to have any meaningful impact on student achievement, and countless students have suffered.

In Michigan, public official’s powers are recognized as fiduciary. They are expected to use these powers to protect, advance, and promote the interest of the public that they serve. The specific scope of an Emergency Manager’s fiduciary duty owed to the local government electorate during a declared fiscal crisis has yet to be fully tested in the courts, but it would be difficult to argue that they are completely immune from accountability for decisions that result in harm to the entity they are appointed to assist. DPS is potentially an example of this, where the appointment of successive Emergency Managers for the express purpose of solving DPS’ financial challenges seemingly had the exact opposite effect and left DPS on the brink of insolvency. This resulted in millions of dollars in damages to both DPS and the City of Detroit, the loss of value of DPS’ real property that will never be recovered, and students who suffered when their education seemingly became less of a priority than the endless financial struggles of DPS.

As a final consideration, it would be presumptuous to assume that the issues that occurred while the state and its agents were in control of DPS would not have occurred if some alternative form of governance had been in place. As many have already observed, many of DPS’ challenges are rooted in the fact that DPS grossly is underfunded, and that the state’s current funding mechanisms are inadequate and dysfunctional. It would therefore be speculative to presume that another governing body, elected or not, would have been able to avoid these pitfalls and somehow address the structural operational and financial issues of DPS.

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60 See Opinion No. 7184, Office of the Attorney General of the State of Michigan, 2006 Mich AG LEXIS 1; See also *Macomb County Prosecuting Attorney v Murphy*, 464 Mich 149; 627 N.W.2d 247 (2001).