



CITY OF DETROIT
OFFICE OF THE EMERGENCY MANAGER

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April 15, 2014

Mr. R. Kevin Clinton
State Treasurer,
Michigan Department of Treasury
Bureau of Local Government Services
4th Floor Treasury Building
430 West Allegan Street
Lansing, MI 48992

Dear Mr. Clinton:

I enclose the quarterly report of the Emergency Manager of the City of Detroit as required by Section 9(5) of the Local Financial Stability and Choice Act (Michigan Public Act 436 of 2012). The report details the financial condition of the City for the quarterly period of January 1, 2014 through March 31, 2014.

Respectfully submitted,

Keyvn D. Orr
Emergency Manager
City of Detroit

Enclosure

cc: Mr. Tom Saxton, Chief Deputy Treasurer
Mr. Edward B. Koryzno, Administrator, Office of Fiscal Responsibility

<u>State Representatives</u>	<u>State Senators</u>
The Hon. Brian Banks	The Hon. Coleman Young, II
The Hon. Alberta Talabi	The Hon. Bert Johnson
The Hon. John Olumba	The Hon. Morris W. Hood, III
The Hon. Rose Mary Robinson	The Hon. Virgil Smith
The Hon. Fred Durhal	The Hon. Tupac A. Hunter
The Hon. Rashida Tlaib	
The Hon. Thomas Stallworth	
The Hon. David Nathan	
The Hon. Harvey Santana	
The Hon. Phil Cavanagh	

QUARTERLY REPORT WITH RESPECT TO THE FINANCIAL CONDITION OF
THE CITY OF DETROIT

April 15, 2014

This quarterly report covers the period from January 1, 2014 through March 31, 2014 (the "Reporting Period") and addresses the financial condition of the City of Detroit.

Local Financial Stability and Choice Act (Michigan Public Act 436 of 2012) ("PA 436")

Section 9(5) [MCL § 141.1549(5)]

The emergency manager shall submit quarterly reports to the state treasurer with respect to the financial condition of the local government in receivership, with a copy to the superintendent of public instruction if the local government is a school district and a copy to each state senator and state representative who represents that local government. In addition, each quarterly report shall be posted on the local government's website within 7 days after the report is submitted to the state treasurer.

Status of the Financial Condition of Detroit
January 1, 2014 – March 31, 2014

Emergency Manager's Comments on the Financial Condition of the City of Detroit

Despite progress in the City's restructuring, the financial condition of the City of Detroit continues to be dire. On July 18, 2013, the City filed for relief under chapter 9 of title 11 of the United States Code (the "Bankruptcy Code") in the United States Bankruptcy Court for the Eastern District of Michigan (the "Bankruptcy Court"). The City's bankruptcy case is captioned *In re the City of Detroit, Michigan*, Case No. 13-53846 (Bankr. E.D. Mich.) (the "Bankruptcy Case"). In December 2013, the Bankruptcy Court determined that the City is eligible to be a debtor in the Bankruptcy Case.

The City has stopped making payments related to unsecured funded debt and legacy liabilities, with the exception of certain retiree healthcare benefits, which the City continued to pay in the ordinary course during the Reporting Period (subject to certain modifications effective as of March 1, 2014), and certain critical vendors. Shortly after the Reporting Period, the City closed a Bankruptcy Court-approved \$120 million postpetition bankruptcy loan to assist in funding various restructuring and reinvestment initiatives (described below).

General Fund Cash Flows and Liquidity Results for the Second Quarter of Fiscal Year 2014

(See Appendix A)

The City's 2014 fiscal year runs from July 1, 2013 through June 30, 2014. At the beginning of the third quarter of fiscal year 2014, the City's General Fund had cash of \$208 million before accumulated property tax distributions in the amount of \$115.5 million, resulting in a net unrestricted cash balance of \$92.6 million. Based upon actual results for the third quarter of fiscal year 2014 (*i.e.*, the three months ended March 28, 2014), the City had positive net cash flow of \$58.9 million. This resulted in a cash balance of \$267.0 million, as of March 28, 2014, before deducting accumulated property tax distributions of \$84.2 million (preliminary estimate), leaving a net ending unrestricted cash balance of \$182.8 million.

During the third quarter, the City continued to make payments related to certain LTGO debt, UTGO debt and certificate of participation interest rate swaps that constitute secured debt. Amounts paid related to these obligations on a cash basis were \$9.8 million, \$1.6 million and \$12.7 million, respectively. While the City has continued to make payments related to health coverage for retirees during the Reporting Period, the General Fund did not make pension contributions to either the General Retirement System ("GRS") or the Police and Fire Retirement System ("PFRS"). Similarly, the City did not make any payments on unsecured LTGO and UTGO bond debt during the Reporting Period.

The unrestricted cash balance exceeded the third quarter forecasted balance by \$13.8 million. When comparing the forecasted and actual cash flows for the third quarter of fiscal year 2014, the major variances were as follows:

- \$19.3 million negative variance in property taxes (net of actual and accrued distributions) related to timing of collections.
- \$7.8 million negative variance in Gaming Taxes due to timing of receipts in connection with creditor negotiations.
- \$20 million positive variance in Other Receipts related to timing of receipts from interagency billings.
- \$6.4 million positive variance in Payroll, Taxes & Deductions due to reductions in headcount.
- \$44 million positive variance in Pension Contributions due to suspended contributions.
- \$44.9 million positive variance in Tax Distributions – UTGO due to timing of payments. However, related amounts owed are accrued in the accumulated property tax distributions reserve of \$84.2 million.
- \$6.7 million negative variance Tax Distributions – TIF due to timing, since payments were projected to be paid in the previous quarter.

Preliminary Unaudited Revenues and Expenditures for the 9 Months Ended March 2014

(See Appendix B)

The revenues and expenditures report includes entries that have not been posted in the general ledger and encumbrances. This manner of presentation provides the most up to date data on revenues and expenditures. Unposted entries are preliminary and subject to review before they are finalized; therefore, actual results will likely be different from the preliminary results presented herein, and those differences may be material.

Preliminary unaudited General Fund revenues and expenditures for the third quarter ended March 31, 2014 result in a surplus of \$43.7 million. Year-to-date revenues are approximately \$34.7 million lower than the last fiscal year mostly related to declining trends in utility users' taxes, licenses charges and general fund contributions, offset by municipal income tax, sales and charges for services and state revenue sharing, relative to the same period in the prior year. Operating expenditures have declined by approximately \$31.5 million, largely due to a reduction in employee headcount, from 9,567 city employees as of March 31, 2013 to approximately 8,980 city employees as of March 31, 2014.

Emergency Manager Actions Regarding Restructuring Process

Background

The Emergency Manager previously submitted quarterly reports pursuant to Section 9(5) of PA 436 dated July 15, 2013, October 15, 2013 and January 15, 2014 (collectively, the "Prior Quarterly Reports" and each, a "Quarterly Report"). As described in the Prior Quarterly Reports, immediately upon his appointment, the Emergency Manager began the process of developing a comprehensive restructuring plan for the City and addressing the City's other urgent needs. The Emergency Manager has taken decisive action to improve public health and safety by taking steps to update outdated and poorly maintained emergency vehicles, information technology infrastructure and facilities and address other

longstanding needs of the City. These activities are described in the Prior Quarterly Reports and include, among other things, opening the Detroit Public Safety Headquarters, hiring a new Chief of Police and developing and pursuing a plan to fix streetlights and address the City's outdated power grid.

To assist in this process, the Emergency Manager spent significant time from the outset of his appointment working with the City's financial and legal advisors to cast a critical eye on all of the City's financial obligations and operational issues to develop a realistic assessment of the City's problems, obstacles, needs and opportunities. As noted in the Prior Quarterly Reports, the goal of this process was to develop a comprehensive plan to: (a) ensure that the City is able to provide for or procure governmental services essential to the health, safety and welfare of its citizens; (b) assure the fiscal accountability and stability of the City; and (c) promote private investment in the City and the revitalization of the community in a sustainable fashion.

One of the first steps was the development of a financial and operating plan for the City (the "Financial and Operating Plan"), which placed the City's challenges in context and defined a series of goals and initiatives. The Financial and Operating Plan, dated May 12, 2013, was submitted to the State Treasurer as required by Section 11(2) of PA 436 on May 13, 2013 and is available on the City's website at <http://www.detroitmi.gov/EmergencyManager/Reports.aspx>.

Continuing to build on these actions, the Emergency Manager and his advisors developed and presented a detailed restructuring proposal to creditors on June 14, 2013 (the "Restructuring Proposal"). The 128-page Restructuring Proposal details a thorough overhaul and restructuring of the City's operations, finances and capital structure. The Restructuring Proposal also proposes recoveries for each creditor group. The proposal was based on ten-year projections that provided a realistic basis for evaluating the City's financial wherewithal to satisfy creditors' claims and achieve the City's restructuring goals. The Restructuring Proposal is described in the first Quarterly Report and is available on the City's website at <http://www.detroitmi.gov/EmergencyManager/Reports.aspx>.

As noted in the Prior Quarterly Reports, following the presentation of the Restructuring Proposal to approximately 150 creditor representatives on June 14, 2013, the City conducted a series of individualized meetings with its organized and represented creditor constituencies to: (a) provide them with additional details on the financial condition of the City; (b) describe key assumptions used to develop the ten-year projections underlying the Restructuring Proposal; (c) provide a forum to answer questions from creditors; (d) solicit responses and counter-proposals from the various constituencies; and (e) negotiate regarding the City's Restructuring Proposal. Despite these efforts, the negotiation of a comprehensive consensual restructuring proved to be impracticable.

On July 18, 2013 (the "Petition Date"), following approval by the Governor, the City filed a voluntary petition commencing the Bankruptcy Case. Along with its voluntary petition, the City filed various other papers, including the Declaration of Kevyn D. Orr in Support of City of Detroit, Michigan's Statement of Qualifications Pursuant to Section 109(c) of the Bankruptcy Code (the "Orr Declaration"). The Orr Declaration explains the history of the City's financial and operational problems, details the dire

circumstances facing the City and provides support for the City's eligibility to be a chapter 9 debtor under the Bankruptcy Code.

On December 5, 2013, the Bankruptcy Court entered (a) its opinion holding that the City is eligible to be a debtor under chapter 9 of the Bankruptcy Code (the "Eligibility Opinion") and (b) an order for relief entitling the City to proceed under chapter 9 (the "Order for Relief" and, together with the Eligibility Opinion, the "Eligibility Order"). A number of objectors filed notices of appeal of the Eligibility Order, and certain of them sought (a) certification of their appeals directly to the United States Court of Appeals for the Sixth Circuit (the "Circuit Court") rather than to the United States District Court for the Eastern District of Michigan (the "District Court") and (b) expedited consideration of their appeals by the Circuit Court. These appeals remain pending, as described further below.

A more detailed description of events before and after the commencement of the Bankruptcy Case is provided in the Prior Quarterly Reports. Additional information regarding these matters is contained in the Disclosure Statement (as defined below). The Orr Declaration, the Eligibility Opinion, the Order for Relief and the Disclosure Statement, along with other Bankruptcy Case filings and other information relevant to the Bankruptcy Case, can be found on the website of the City's claims and noticing agent at www.kccllc.net/Detroit.

General Actions During the Reporting Period

During the Reporting Period, the Emergency Manager, his staff and outside advisors have continued to dedicate significant time and energy to addressing the City's financial and operational emergency. Just as with respect to prior reporting periods, meetings with interested parties, state and federal government officials, professional advisors and creditors occur numerous times each week, if not daily.

In support of the City's restructuring, the Emergency Manager issued several important orders that promote the health, safety and welfare of the City's residents and visitors. These orders also were designed to assist the Emergency Manager in his efforts to analyze and address the factors and circumstances contributing to the City's financial emergency. Since the submission of the third Quarterly Report, the Emergency Manager has entered orders consistent with PA 436, including an order approving a resolution adopted by the Board of Commissioners of the Detroit Water and Sewerage Department authorizing publication of a notice of intent to issue certain sewage disposal system revenue bonds. In addition, during the Reporting Period, the Emergency Manager issued an order suspending, pending further order or written directive of the Emergency Manager, the implementation of Order No. 21, which suspended the accrual of benefits under the City's pension fund for non-public safety workers (*i.e.*, the GRS), and replaced the GRS with a new qualified defined contribution plan. These orders, in addition to all prior and future orders, are available on the City's website at <http://www.detroitmi.gov/EmergencyManager/Orders.aspx>.

Activities in the Bankruptcy Case

The Emergency Manager continues to move the Bankruptcy Case forward as expeditiously as possible to complete an adjustment of the City's debts under the Bankruptcy Code by no later than the fall of 2014.

Concluding the Bankruptcy Case in a timely and efficient manner is important to the City's revitalization and reinvestment activities because it will free the City from burdensome and unsustainable debt obligations and allow the City to reinvest in operations and infrastructure, which in turn will attract new businesses and residents to the City and promote the health, safety and welfare of the public.

Certain of the primary activities in the Bankruptcy Case during the Reporting Period are summarized below:

Plan of Adjustment and Disclosure Statement

The Bankruptcy Court set a deadline of March 1, 2014 for the City to file a plan of adjustment in the Bankruptcy Case. On February 21, 2014, the Emergency Manager filed the Plan for the Adjustment of Debts of the City of Detroit (Docket No. 2708) (as amended, modified or supplemented from time to time, the "Plan") and the related Disclosure Statement with Respect to Plan for the Adjustment of Debts of the City of Detroit (Docket No. 2709) (as amended modified or supplemented from time to time, the "Disclosure Statement"). Amended versions of the Plan and the Disclosure Statement were filed on March 31, 2014 (Docket Nos. 3380 and 3382, respectively) and (after the Reporting Period) further amended versions of the Plan and the Disclosure Statement will be filed in April 2014. The Plan provides for the resolution of a variety of complex financial and operational issues faced by the City. The Emergency Manager believes that adjustment of the City's debts pursuant to the Plan will provide the best recovery for creditors of the City on a fair and equitable basis, while simultaneously allowing for meaningful and necessary investment in the City. The Plan contemplates the City's emergence from chapter 9 this year and represents a crucial step toward the City's rehabilitation and recovery from its decades-long downward spiral.

The Plan includes settlements that the Emergency Manager believes will inure to the benefit of the City's creditors and its residents. For example, the Plan incorporates a settlement of difficult issues relating to the Detroit Institute of Arts ("DIA"), which settlement (a) is expected to yield at least \$466 million to provide a source of recovery for the approximately 33,000 individuals who participate in the City's retirement systems (the GRS and the PFRS) and (b) will free up other funds for distribution to other creditors. The Plan also incorporates, among other things, (a) a settlement with the State of Michigan to further assist in funding pension claims (sometimes referred to with the DIA settlement as the "Grand Bargain"), (b) the settlement of swap claims, (c) a settlement of claims related to unlimited tax general obligation bonds (as described below) and (d) a settlement of certain claims of police and firefighter retirees (as described below).

Except in the case of subordinated claims (which receive no recovery), the Plan provides a recovery to all classes of Claims consistent with the legal rights and priorities of each creditor group. The Plan also allows for investment in the City of approximately \$1.5 billion over ten years, which the Emergency Manager believes is critical and meaningful to, among other things: (a) provide basic, essential services to City residents; (b) attract new residents and businesses to foster growth and redevelopment; (c) reduce crime; (d) demolish blighted and dangerous properties; (e) provide functional streetlights that are aligned with the current population footprint; (f) improve information technology systems, thereby

increasing efficiency and decreasing costs; and (g) otherwise set the City on a path toward a better future. The Emergency Manager believes that the Plan gives the City the best chance of effectively adjusting its debts and reestablishing itself as a prosperous and productive American city.

The Disclosure Statement contains detailed information about the terms of the Plan, projected recoveries to creditors thereunder, the settlements incorporated into the Plan, the risk factors associated with the Plan, the tax consequences of the restructuring contemplated by the Plan and various other matters. The Disclosure Statement also provides detail about the events leading up to, and the activities in, the Bankruptcy Case.

The Bankruptcy Court has scheduled a hearing on approval of the Disclosure Statement for April 17, 2014. The deadline for voting on the Plan currently is scheduled to be June 30, 2014, and the hearing on confirmation of the Plan is scheduled to commence on July 16, 2014.

Swap Settlement

Prior to the Petition Date, the Emergency Manager reached a consensual resolution of certain interest rate swap agreements (collectively, the "Swap Agreements") to eliminate one of the City's largest secured obligations at a discount and ensure ongoing access to critical casino revenues that were pledged to support the Swap Agreements (the "Casino Revenues"). This agreement was memorialized in that certain Forbearance and Optional Termination Agreement (the "FOTA") between the City and the counterparties to the Swap Agreements (collectively, the "Swap Counterparties"). On the Petition Date, the City filed a motion (Docket No. 17) (the "First Swap Settlement Motion") seeking approval of, and authorization to assume, the FOTA.

At the direction of the Bankruptcy Court, following extensive discovery and an evidentiary hearing regarding the First Swap Settlement Motion, the parties engaged in additional mediation relating to the Swap Agreements in December 2013. This resulted in an improved settlement for the benefit of the City, establishing a fixed termination payment amount for the swaps of \$165 million (reduced from an estimated \$230 million). This enhanced settlement was presented to the Bankruptcy Court. On January 17, 2014, the Bankruptcy Court issued an order (Docket No. 2511) (the "First Swap Settlement Order") declining to grant the relief requested in the First Swap Settlement Motion (as modified by the enhanced settlement terms). According to the Bankruptcy Court, the proposed reduced optional termination payment of \$165 million exceeded the range of reasonableness because the City had a reasonable likelihood of success on certain legal defenses. Thereafter, on February 6, 2014, the City filed a notice of termination of the FOTA (Docket No. 2655).

In light of the Bankruptcy Court's denial of the First Swap Settlement Motion, and informed by the Court's views with respect to the probability of success on certain legal defenses, the Emergency Manager and his advisors considered appropriate next steps that would safeguard the City and ensure continued access to the City's critically necessary Casino Revenues. The Emergency Manager actively prepared to pursue litigation against the Swap Counterparties to protect the interests of the City and its residents. At the same time, the City continued to engage the Swap Counterparties in settlement discussions at the direction of the Emergency Manager. As a result of these discussions, the City

reached a new settlement with the Swap Counterparties. On March 3, 2014, the City filed the Motion of Debtor for Entry of an Order, Pursuant to Section 105(a) of the Bankruptcy Code and Bankruptcy Rule 9019, Approving a Settlement and Plan Support Agreement and Granting Related Relief (Docket No. 2802) (the "Second Swap Settlement Motion") seeking approval of a new settlement agreement with the Swap Counterparties (the "Swap Settlement Agreement").

Pursuant to the Swap Settlement Agreement, the City would continue to make quarterly payments due to the Swap Counterparties under the Swap Agreements up to the aggregate sum of \$85 million in cash – less a credit of approximately \$12.6 million that is currently being held by the Swap Counterparties in segregated accounts – in full satisfaction of the claims between the parties. This represents an approximately 70 percent reduction in the termination payment amount otherwise called for in the swap agreements and would allow the City to satisfy this liability in manageable amounts over time, rather than in a lump sum. A number of objections and other responses were filed to the Second Swap Settlement Motion. An evidentiary hearing before the Bankruptcy Court regarding the Second Swap Settlement Motion was held on April 3, 2014. On April 11, 2014, the Bankruptcy Court announced its ruling granting the Second Swap Settlement Motion and approving the Swap Settlement Agreement. The terms of the Swap Settlement Agreement have been incorporated into the Plan.

Postpetition Financing

To fund the proposed settlement with the Swap Counterparties described in the First Swap Settlement Motion and to obtain cash necessary to make critical reinvestments in the City, the City determined that it needed new postpetition financing. The City received a commitment for new bankruptcy financing from Barclays Capital Inc. ("Barclays"). On November 5, 2013, the City filed a motion in the Bankruptcy Case (Docket No. 1521) (the "Postpetition Financing Motion") for, among other things, authorization to obtain senior secured postpetition financing from Barclays on a superpriority basis.

As originally proposed, the postpetition financing was for a total of \$350 million in new borrowing comprised of two series of secured bonds — the "Swap Termination Bonds" in the amount of \$230 million (the "Swap Termination Loan") and the "Quality of Life Bonds" in the amount of \$120 million (the "Quality of Life Loan"). After filing the Postpetition Financing Motion, the City renegotiated the settlement with the Swap Counterparties, which resulted in the requested Swap Termination Loan being reduced to \$165 million to reflect the enhanced swap settlement terms (with the requested Quality of Life Loan remaining at \$120 million). Thus, as a result of the renegotiated settlement, the total amount of secured postpetition financing sought by the City pursuant to the Postpetition Financing Motion was reduced to \$285 million, with Barclays' consent.

On January 17, 2014, in connection with the First Swap Settlement Order, the Bankruptcy Court declined to approve the proposed Swap Termination Loan that was to be used to finance the payment of the swap settlement that was denied by the Bankruptcy Court. In its ruling on the Postpetition Financing Motion, however, the Bankruptcy Court stated that it would approve in principle the Postpetition Financing Motion with respect to the Quality of Life Loan, thereby potentially authorizing

the City to obtain postpetition secured financing of up to \$120 million to address the City's restructuring initiatives, subject to certain conditions.

Following this ruling, the City and Barclays engaged in discussions about proceeding with only the Quality of Life Loan. Certain terms and conditions of the Quality of Life Loan required revision due to the denial of the swaps settlement, particularly because the City would not be in a position to grant first priority liens in the Casino Revenues. On March 6, 2014, the City filed a notice of presentment in the Bankruptcy Court (Docket No. 2921) of a proposed order (the "Financing Order") to approve a revised Quality of Life Loan of \$120 million (the "Revised Quality of Life Loan"). On April 2, 2014, the Bankruptcy Court entered the Financing Order (Docket No. 3607) approving the Revised Quality of Life Loan and thereby authorizing the City to issue up to \$120 million in Quality of Life Bonds. The Revised Quality of Life Loan closed on April 8, 2014.

The proceeds of the Revised Quality of Life Loan will be used to advance certain key investment initiatives of the City, including, but not limited to, essential investments in blight removal, public safety and technology infrastructure. The postpetition financing received under the Revised Quality of Life Loan will empower the City to take critical steps in its effort to revitalize and improve public health, safety and welfare. Although the funds provided under the Revised Quality of Life Loan will not address all of the City's reinvestment initiatives, the Revised Quality of Life Loan will kick-start a long-term reinvestment process at the rate of approximately \$20 million per month of net reinvestment activity during the current fiscal year. Without these borrowed funds, there is a material risk that the City would have had to cut back substantially or eliminate its reinvestment efforts in the near-term, and the City's ability to invest in the future would continue to have been hamstrung and imperiled by the City's ongoing financial constraints.

Modifications to Healthcare

To address the City's need to act quickly to alleviate its dire financial situation and cash position, the Emergency Manager determined that the City needed to make changes to the benefit plan options and health insurance benefits that it would offer to active and retired employees in 2014.

In general, the City made changes to medical coverage in 2014 designed to provide active employees with coverage that would be equivalent to "Gold" level coverage under the Patient Protection and Affordable Care Act (the "Affordable Care Act"). Previously, most active employees in the City were receiving coverage that would be equivalent to "Platinum" level coverage under the federal Affordable Care Act. The revised plans provide an HMO and a PPO option. All active employees are required to pay 20% of the premium cost for health care coverage, the same share as most paid in 2013. The City offered one dental and one vision plan for 2014. In addition, beginning January 1, 2014, the City offered all health care plan eligible employees the option to elect participation in a flexible spending account. Although annual deductibles and out-of-pocket coinsurance maximums have increased, most employees are expected to pay less for healthcare coverage in 2014 than they did in 2013.

Effective March 1, 2014, the Emergency Manager modified the health insurance coverage offered to retirees. Medicare eligible Retirees are now able to select one of three Medicare Advantage insurance

plans that include health and drug benefits for which the City pays most or all of the premium. Except with respect to one particular plan, the monthly premium cost to the Medicare eligible retiree was zero. Non-Medicare eligible retirees are required to obtain their own health insurance coverage through, for example, (a) the Health Insurance Marketplaces created by the Affordable Care Act, (b) the retiree's current employer or (c) his or her spouse's employer. For most retirees who are not eligible to receive Medicare benefits, the Emergency Manager agreed that the City would provide a stipend of \$125 per month (\$300 or \$400 per month for duty disabled non-Medicare retirees, depending upon whether the disabled person is a uniform retiree). The City no longer subsidizes dental and vision coverage for retirees.

These healthcare changes are projected to generate necessary savings for the benefit of the City.

Mediation

In addition to mediation of the swap settlement disputes as described above, substantial time and effort has been devoted by the Emergency Manager and his staff and advisors to negotiating other key restructuring issues through a mediation program established by the Bankruptcy Court to facilitate these efforts. In particular, Bankruptcy Judge Steven W. Rhodes appointed District Court Chief Judge Gerald E. Rosen as lead mediator for the Bankruptcy Case. In turn, Judge Rosen appointed six additional mediators, each focusing on different elements of the City's restructuring and reorganization activities. To date there have been multiple, regular mediation sessions and numerous written submissions related to, among other things, the City's core restructuring and reorganization initiatives outlined in the Restructuring Proposal, as well as labor and pension matters. The Emergency Manager continues to embrace the mediation process, which is ongoing.

As part of the formal mediation process and in separate discussions, the City has continued to engage in ongoing dialogue with its unions, pension systems, debt holders (trustees, individual holders and ad hoc groups), the Official Committee of Retirees appointed in the Bankruptcy Case (the "Retiree Committee") and other interested parties to advance key restructuring issues. The Emergency Manager and his staff and advisors will continue to meet with creditors and interested parties with the goal of reaching, to the fullest extent possible, consent on the terms of the Plan to address the City's operational and financial restructuring needs.

Retired Detroit Police and Fire Fighters Association Settlement

Following the end of the Reporting Period, the mediation process described above led to an agreement between the City and the Retired Detroit Police and Fire Fighters Association ("RDPFFA") with respect to the treatment of pension and health benefits for retired Detroit police officers and firefighters. The agreement with the RDPFFA is the first agreement that the City has reached with a group of its retired workers and is particularly significant as the RDPFFA is the one of the City's oldest and largest employee associations, dating back to 1946. It has approximately 6,500 members, which is more than 80% of Detroit's eligible retired police officers and firefighters.

The mediated agreement – approved unanimously by the RDPFFA’s board on April 15, 2014 – is contingent upon full funding of the so-called Grand Bargain resolving pension issues. Under the agreement with RDPFFA, the uniformed retirees would experience no cuts to their current pension benefits and would receive almost half of their cost of living adjustment (COLA) benefits going forward. Further, depending upon the performance of the PFRS, there is the possibility of full restoration of COLA benefits under the Plan. In addition, a separate PFRS Voluntary Employee Beneficiary Association plan (“VEBA”) for PFRS retiree healthcare will be established. Finally, the PFRS retirees will have a meaningful voice and retain a vote on the new pension board.

Claims Matters

Prior to the Reporting Period, on November 21, 2013, the Bankruptcy Court entered an order establishing February 21, 2014 at 4:00 p.m., Eastern Time, as the deadline for most of the City’s creditors to file proofs of claim in the Bankruptcy Case (the “Claims Bar Date”). More than 3,600 claims were filed by the Claims Bar Date, and the City is in the early stages of the process of reviewing and reconciling the timely filed claims against its books and records.

During the Reporting Period, the Emergency Manager has taken other steps toward resolving and quantifying contingent, unliquidated and disputed claims against the City in the Bankruptcy Case. On December 24, 2013, the Bankruptcy Court entered an order establishing alternative dispute resolution procedures (collectively, the “ADR Procedures”) to promote the efficient liquidation of tort claims and other claims designated by the City. The City is in the process of implementing the ADR Procedures in connection with its review of filed claims.

Bankruptcy Court Litigation

During the Reporting Period, the Emergency Manager, through his staff and advisors, also has been required to respond to several lawsuits commenced or continued in the Bankruptcy Court by parties in interest in the Bankruptcy Case, many of whom also are involved in ongoing mediation proceedings and other restructuring negotiations with the City.

Eligibility Appeals. As described above, the Bankruptcy Court’s Eligibility Order has been appealed by numerous parties, with certain appellants seeking a direct appeal to the Circuit Court on an expedited basis. On February 21, 2014, the Circuit Court entered orders granting the direct appeals of the Eligibility Order, but declining to expedite the appeals at that time. Certain appellants filed motions to expedite the briefing schedule and oral argument, which were denied, and the City has been authorized to file a consolidated appellate brief addressing issues raised in each of the seven related appeals. A briefing schedule has been established, and briefing is scheduled to begin this month in the Circuit Court. All appeals of the Eligibility Order pending in the District Court are indefinitely stayed in light of the pending proceedings before the Circuit Court.

City of Detroit, Michigan v. Syncora Guarantee Inc., et al., Adv. Proc. No. 13-04942 (the “Casino Revenue Proceeding”). On August 8, 2013, the District Court referred to the Bankruptcy Court a lawsuit originally commenced by the City in the Wayne County Circuit Court seeking a declaration that Syncora is

prohibited from taking any action to block the City's access to the Casino Revenues. On November 25, 2013, the Bankruptcy Court entered a stipulated order that, among other things, stayed the Casino Revenue Proceeding for a period of 60 days from the date of the Bankruptcy Court's order. The stipulated stay expired on January 24, 2014 and on January 27, 2014, Syncora filed a motion to withdraw the reference of the Casino Revenue Proceeding to the Bankruptcy Court. As of the date hereof, Syncora's motion has been fully briefed, but has not been determined by the District Court.

Syncora Guarantee Inc. v. UBS AG, et al., Adv. Proc. No. 13-05395 (the "Swap Settlement Proceeding"). Prior to the Petition Date, Syncora commenced the Swap Settlement Proceeding in New York state court seeking to enjoin the Swap Counterparties from entering into the FOTA. The Swap Settlement Proceeding was removed to the United States District Court for the Southern District of New York and then transferred to the District Court. On October 10, 2013, the City filed a motion to intervene in the Swap Settlement Proceeding. On January 29, 2014, the Bankruptcy Court granted the City's motion to intervene. The Swap Counterparties filed a motion to dismiss the Swap Settlement Proceeding and Syncora filed (a) a motion seeking a determination that the proceeding was a non-core proceeding with respect to which the Bankruptcy Court lacks authority to enter final judgment and (b) a motion for summary judgment. On February 9, 2014, Syncora filed a notice with the Bankruptcy Court dismissing the Swap Settlement Proceeding without prejudice.

The Official Committee of Retirees of the City of Detroit, Michigan, et al. v. The City of Detroit, Michigan, et al., Adv. Proc. No. 13-05244 (the "First Retiree Proceeding"). On October 22, 2013, the Retiree Committee, the Detroit Retired City Employees Association, the Retired Detroit Police and Fire Fighters Association and AFSCME Subchapter 98, City of Detroit Retirees (collectively, the "Retiree Representatives") filed a complaint against the City and the Emergency Manager seeking an order reinstating certain retiree health benefits modified by order of the Emergency Manager and enjoining the City and the Emergency Manager from making further modifications to retiree health benefits. During the pendency of the First Retiree Proceeding, the parties were engaged in mediation before Chief Judge Rosen of the District Court. As a result of negotiations between the parties (including the temporary deferral of proposed changes to retiree benefits), on November 8, 2013, the plaintiffs filed a notice of dismissal of the First Retiree Proceeding without prejudice. On January 9, 2014, the Retiree Representatives commenced a second proceeding against the City and the Emergency Manager, captioned The Official Comm. of Retirees of the City of Detroit, Michigan, et al. v. The City of Detroit, Michigan, et al., (Adv. Proc. No. 14-04015) (the "Second Retiree Proceeding"), seeking a preliminary injunction to enjoin the defendants from implementing certain retiree healthcare modifications announced by the Emergency Manager effective March 1, 2014. By a settlement agreement effective February 14, 2014, the parties agreed to certain modifications to the revised retiree health benefits set forth in the 2014 Retiree Health Care Plan. The settlement agreement modifications include an obligation by the City to provide additional stipend amounts during a portion of 2014 to non-Medicare eligible retirees and to offer Medicare eligible retirees certain additional options. On March 31, 2014, the Bankruptcy Court entered a stipulated order of dismissal (Adv. Proc. Docket No. 48).

National Public Finance Guarantee Corp., et al. v. City of Detroit, Michigan, et al., Adv. Proc. No. 13-05309 (the "UTGO Proceeding"). On November 8, 2014, monoline insurers National Public Finance

Guarantee Corporation (“National”) and Assured Guaranty Municipal Corporation (“Assured”) filed a complaint against the City, the Emergency Manager and the City Finance Director, Deputy Finance Director and Treasurer seeking a declaratory judgment that the City is required to segregate certain *ad valorem* tax revenues for the ultimate payment of amounts due under the City’s unlimited tax general obligation bonds (the “UTGO Bonds”).

In papers filed with the Bankruptcy Court, the City has disputed the plaintiffs’ characterization of the City’s obligations with respect to the UTGO Bonds. The City took the position that the UTGO Bond debt is a general unsecured obligation. The City also took the position that the bondholders are precluded from seeking relief, both because there is no private right of action under Revised Municipal Finance Act of 2001, MCL §§ 141.2101, *et seq.* (the “Municipal Finance Act”) and because section 904 of the Bankruptcy Code bars the Bankruptcy Court from entering an order that would interfere with the City’s political or governmental powers or with its property or revenues. Further, the City argued that the UTGO Bonds are backed only by a promise to repay them either from general revenue or ad valorem taxes, and not by a lien on tax revenue. Finally, the City contested the plaintiffs’ assertion of a property interest in the ad valorem tax revenues. On February 19, 2014, the Bankruptcy Court conducted a hearing on the City’s motion to dismiss the UTGO Proceeding. Pending the Bankruptcy Court’s determination, the Bankruptcy Court ordered the parties to engage in further mediation of these issues. This mediation resulted in a resolution that will be reflected in the second amended version of the Plan. Under the settlement, the holders of UTGO Bonds will (a) exchange certain of their existing bonds in the principal amount of \$287.5 million for bonds newly-issued by the Michigan Finance Authority on the same financial terms as such existing bonds and (b) assign their right to payment on the remainder of the existing bonds to an entity designated by the City. As of the date of this Quarterly Report, the UTGO Proceeding remains pending. Pursuant to the settlement, however, the UTGO Proceeding will be stayed pending the occurrence of the effective date of the Plan, whereupon the City and the settling bond insurers will ask the Bankruptcy Court to dismiss the UTGO Proceeding.

Ambac Assurance Corp. v. City of Detroit, Michigan, et al., Adv. Proc. No. 13-05310 (the “UTGO/LTGO Proceeding”). Also on November 8, 2014, Ambac Assurance Corporation (“Ambac”) filed a complaint against the City, the Emergency Manager and the City Finance Director, Deputy Finance Director and Treasurer seeking substantially similar relief to that sought in the UTGO Proceeding, but with respect to four series of the City’s limited tax general obligation bonds (the “LTGO Bonds”) in addition to certain series of the UTGO Bonds. Ambac alleges that the Emergency Manager and the City are obligated to use general tax revenues collected within the City’s charter, statutory or constitutional limitations to service the LTGO Bonds. The Emergency Manager disputes Ambac’s characterization of the City’s obligations with respect to the LTGO Bonds. The Emergency Manager took the position that the LTGO Bonds merely create a “first budget obligation” under the Municipal Finance Act, which creates a priority inconsistent with chapter 9 distribution rules (and therefore is ineffective in chapter 9) and does not create a lien or trust. Moreover, although Ambac has not expressly asserted in the UTGO/LTGO Proceeding the argument that all other unsecured claims are subordinated to the LTGO Bond debts, the City has taken the position that any such subordination can be accomplished only through an inter-creditor agreement; *i.e.*, the City cannot agree to make certain creditors’ claims subordinate to the

claims of another creditor. On February 19, 2014, the Bankruptcy Court conducted a hearing on the City's motion to dismiss the UTGO/LTGO Proceeding. Pending the Bankruptcy Court's determination, the Bankruptcy Court ordered the parties to engage in further mediation of these issues. As noted above, this mediation resulted in a resolution that will be reflected in the second amended version of the Plan with respect to the UTGO Bonds. Under the settlement, the holders of UTGO Bonds will (a) exchange certain of their existing bonds in the principal amount of \$287.5 million for bonds newly-issued by the Michigan Finance Authority on the same financial terms as such existing bonds and (b) assign their right to payment on the remainder of the existing bonds to an entity designated by the City. As of the date of this Quarterly Report, the UTGO/LTGO Proceeding remains pending.

Appendices

- A. Cash Flow Actuals and variance to Forecast for the Period January-March 2014
- B. Preliminary Unaudited Revenues and Expenditures for 9 Months Ended March 2014

\$ in millions	FY 2014		
	Forecast	Actual	Variance
	Q3	Q3	Q3
Operating Receipts			
Property taxes	\$ 164.7	\$ 145.4	\$ (19.3)
Income & utility taxes	74.5	73.5	(0.9)
Gaming taxes	47.1	39.3	(7.8)
Municipal service fee to casinos	1.8	1.7	(0.1)
State revenue sharing	61.4	63.6	2.2
Other receipts	86.4	106.4	20.0
Refinancing proceeds	-	-	-
Total operating receipts	435.9	429.9	(6.0)
Operating Disbursements			
Payroll, taxes, & deductions	(84.1)	(77.8)	6.4
Benefits	(43.6)	(44.9)	(1.3)
Pension contributions	(44.0)	-	44.0
Subsidy payments	(18.9)	(19.8)	(0.9)
Distributions - tax authorities	(92.2)	(91.6)	0.6
Distributions - UTGO	(44.9)	-	44.9
Distributions - TIF	-	(6.7)	(6.7)
Income tax refunds	(1.2)	(1.5)	(0.3)
A/P and other miscellaneous	(97.3)	(106.2)	(8.9)
Sub-total operating disbursements	(426.3)	(348.5)	77.8
POC and debt related payments	(17.3)	(22.5)	(5.2)
Total disbursements	(443.6)	(371.0)	72.6
Net cash flow	(7.7)	58.9	66.6
Beginning cash balance ¹	\$ 208.0	\$ 208.0	-
Net cash flow	(7.7)	58.9	66.6
Cash before required distributions	\$ 200.4	\$ 267.0	\$ 66.6
Accumulated property tax distributions	(31.4)	(84.2)	(52.8)
Cash net of distributions	\$ 169.0	\$ 182.8	\$ 13.8
<i>Memo:</i>			
Refunding bond proceeds in escrow	59.5	86.9	27.4
Reimbursements owed to other funds	tbd	tbd	

Footnote:

¹ The beginning cash balance as of Jan 1, 2014 has been revised from the preliminary ending balance shown in the Q2 Emergency Manager report due to a deposit in transit, which was not reflected in the preliminary ending balance for Q2.

<i>(\$ in millions)</i>	9 Months Ended Mar-13	9 Months Ended Mar-14	FY14 - FY13 Difference
Revenues			
Property Taxes	\$ 115.7	\$ 109.1	\$ (6.6)
Municipal Income Tax	172.9	183.6	10.6
Wagering Taxes	134.1	125.5	(8.6)
Utility Users' and other taxes	23.6	7.2	(16.4)
Licenses, Permits and Inspection Charges	10.5	4.9	(5.6)
State Revenue Sharing	154.6	159.3	4.7
Sales and Charges for Services	103.5	108.1	4.7
Revenue from Use of Assets	3.5	4.9	1.4
Parking/court fines and other revenue	25.9	29.3	3.4
General Fund and Other Contributions	66.7	38.7	(27.9)
Grant Revenue	31.8	37.3	5.6
Transfers in	-	-	-
Total revenues	842.6	807.9	(34.7)
Expenditures			
Salaries & Wages	(223.0)	(193.3)	29.6
Overtime	(20.9)	(25.9)	(5.1)
Pensions	(103.6)	(93.6)	10.0
Benefits	(164.3)	(151.5)	12.8
Professional and contractual services	(46.0)	(107.4)	(61.4)
Materials & Supplies	(41.8)	(38.4)	3.5
Utilities	(10.0)	(12.5)	(2.5)
Purchased Services	(3.6)	(9.0)	(5.4)
Risk management and insurance	(87.7)	(27.8)	59.9
Other expenses	(24.7)	(32.3)	(7.6)
Debt Service	(5.0)	(4.8)	0.2
Contributions	(2.1)	(2.5)	(0.4)
Transfers Out	(69.3)	(71.4)	(2.2)
Total expenditures	(801.9)	(770.4)	31.5
Deficit (excl. financing proceeds)	40.8	37.5	(3.2)
Financing proceeds	149.7	6.2	(143.5)
Total surplus (deficit)	\$ 190.5	\$ 43.7	\$ (146.7)