



Assurance Inc. (“Assured,” and together with National, “Plaintiffs”), by and through their respective undersigned attorneys, pursuant to Federal Rule of Bankruptcy Procedure 7001(2) and (9), seek a declaratory judgment to determine Plaintiffs’ rights and interests in, and Defendants’ obligations with respect to, voter-approved *ad valorem* taxes the City of Detroit (the “City”) must levy, collect, and use for the sole purpose of paying principal of and interest on the Unlimited Tax Bonds (as defined herein).

### **INTRODUCTION**

1. Having issued hundreds of millions of dollars of unlimited tax general obligation bonds (collectively, the “Unlimited Tax Bonds”) to fund vital capital improvements identified by the Mayor and the City Council of Detroit (the “City Council”), the City is now unlawfully diverting voter-approved *ad valorem* taxes the City must levy, collect, and use for the sole purpose of paying principal of and interest on the Unlimited Tax Bonds.

2. Unique among the City’s financial obligations, the Unlimited Tax Bonds were issued only after the enactment of authorizing resolutions by the City Council, the City’s legislative body, and approval by a majority of the voters in

city-wide elections establishing a pledge of *ad valorem* taxes, as security, to repay these obligations exclusively.<sup>1</sup>

3. In approving each bond referendum, the City's voters authorized the City to exceed the otherwise applicable maximum rate for *ad valorem* taxes contained in article IX, section 6 of the Michigan Constitution (attached hereto as Exhibit B), state statutes, and the City's Charter. Because the City had reached the maximum constitutional, statutory, and charter tax rate at the time the Unlimited Tax Bonds were issued, the City, in the absence of necessary voter approval, would have had no authority to levy and collect these additional *ad valorem* taxes.

4. Further, pursuant to (i) Chapter 141 of the Michigan Public Acts, including Act 34 of the 2001 Revised Municipal Finance Act, Michigan Compiled Laws ("MCL") § 141.2101 *et seq.* ("Act 34," attached hereto as Exhibit C) and Act 189 of the 1979 Unlimited Tax Election Act, MCL § 141.161 *et seq.* ("Unlimited Tax Election Act," attached hereto as Exhibit D), and (ii) the six resolutions and supplemental resolutions adopted by the City Council on March 3, 1999, April 6, 2001, June 13, 2001, July 24, 2002, July 6, 2005, November 17, 2006

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<sup>1</sup> Attached as Exhibit A is a true and correct copy of six ballot questions seeking voter approval of the specific capital projects that were financed or refinanced with a portion of the proceeds of the Unlimited Tax Bonds. Similar ballot questions were approved for each capital project that the City financed or refinanced with Unlimited Tax Bonds.

(collectively, the “Resolutions,” attached hereto as Exhibit E), Michigan law requires the City to:

- levy *ad valorem* taxes for the exclusive purpose of repaying the Unlimited Tax Bonds, without limitation as to rate or amount, and in the amount necessary to repay the obligations—taxes which are separate from and in addition to other *ad valorem* taxes the City is authorized to levy (the “Unlimited Tax Levy”);
- collect the *ad valorem* taxes levied for Unlimited Tax Bond debt service and deposit such taxes in segregated debt retirement funds (the “Debt Retirement Funds”); and
- use the *ad valorem* taxes only to pay principal of and interest on the Unlimited Tax Bonds.

5. Under Michigan law, the City has no equitable or beneficial property interest in the *ad valorem* taxes levied and pledged specifically to secure the repayment of the Unlimited Tax Bonds. Those *ad valorem* taxes (the “Restricted Funds”) are restricted by law and cannot be levied, collected, or used by the City for any purpose other than satisfying the City’s payment obligations with respect to outstanding Unlimited Tax Bonds. Thus, the taxes deposited in the Debt Retirement Funds are Restricted Funds in which the Bondholders and Plaintiffs have equitable and beneficial property interests, and which are not legally available

to the City's general creditors. Further, the Restricted Funds are impressed with a statutory lien as defined in section 11 U.S.C. § 101(53) and, in addition, constitute "special revenues" as defined in 11 U.S.C. § 902(2)(E).

6. On October 1, 2013, the City defaulted on its obligation to make nearly \$9.4 million in interest payments on the Unlimited Tax Bonds, including about \$2.3 million and \$4.2 million in interest payments due on the Unlimited Tax Bonds insured by National and Assured, respectively. The paying agent, as defined in Section 601 of the Resolutions (the "Paying Agent"), made claims under the respective municipal bond insurance policies in such amounts, which were duly paid by National and Assured. Thus, National and Assured are subrogated to the rights of the holders of the Unlimited Tax Bonds (the "Bondholders") and hold direct claims against the City in such amounts.

7. The City has stated publicly that it intends to continue to levy and collect the Restricted Funds, but that it will not segregate the Restricted Funds. The City also has indicated that postpetition it is using and intends to continue to use the Restricted Funds for payment of its general operations. This conduct violates Michigan law (including the express terms of Act 34), as well as the Takings Clause of the Fifth Amendment to the United States Constitution, which is applicable to the City through the Fourteenth Amendment to the United States Constitution.

8. In Count One, Plaintiffs seek a declaratory judgment that under Michigan law the *ad valorem* taxes collected under the Unlimited Tax Levy are restricted by law and cannot be levied, collected, or used by the City for any other purpose except to satisfy the City's payment obligations with respect to outstanding Unlimited Tax Bonds.

9. In Count Two, Plaintiffs seek a declaratory judgment that (i) the City is a conduit for the Restricted Funds and lacks any equitable or beneficial property interest in the Restricted Funds, and (ii) the Bondholders and Plaintiffs, as the Bondholders' subrogees, have equitable and beneficial property interests in the Restricted Funds.

10. In Count Three, Plaintiffs seek a declaratory judgment that the Bondholders and Plaintiffs, as the Bondholders' subrogees, have a statutory lien on the Restricted Funds within the meaning of 11 U.S.C. § 101(53).

11. In Count Four, Plaintiffs seek a declaratory judgment that the Bondholders and Plaintiffs, as the Bondholders' subrogees, have a lien on the Restricted Funds and that the Restricted Funds are special revenues within the meaning of 11 U.S.C. § 902(2)(E) that must be applied in accordance with 11 U.S.C. §§ 922(d) and 928.

12. In Count Five, Plaintiffs seek a declaratory judgment that the City's diversion of the Restricted Funds or grant of any postpetition interest in the

Restricted Funds to any creditor or any other person or any other impairment of the Bondholders' and Plaintiffs' property interests in the Restricted Funds, without just compensation, is an unlawful taking under the Fifth and Fourteenth Amendments to the United States Constitution.

13. In Count Six, Plaintiffs seek a declaratory judgment that, under Michigan law, as *ad valorem* taxes are collected under the Unlimited Tax Levy, the Restricted Funds must be (i) segregated and deposited, as allocable to each series of Unlimited Tax Bonds, into the related Debt Retirement Funds, and (ii) not commingled with other funds of the City or used for any purpose other than repaying the Bondholders (or Plaintiffs as the Bondholders' subrogees).

14. Plaintiffs request only declarations of Plaintiffs' rights and interests in, and Defendants' obligations with respect to, the Restricted Funds as determined by state law and the United States Constitution. As a result, and because the City has no equitable or beneficial property interest in the Restricted Funds, 11 U.S.C. § 904 is not implicated by this Complaint, and this Court has the constitutional and statutory authority to award the relief requested herein. Moreover, 11 U.S.C. § 904 does not prohibit the Court from entering declaratory relief against any Individual Defendants.

## PARTIES

15. Plaintiff National Public Finance Guarantee Corporation is a New York corporation with its principal place of business at 113 King Street, Armonk, New York 10504. National is a monoline insurer that provides financial guarantees to the U.S. public finance market. National insures approximately \$2.4 billion in principal amount of outstanding bonds issued by the City, including water supply system bonds, sewage disposal system bonds, and Unlimited Tax Bonds. The Unlimited Tax Bonds are the only bonds insured by National that are at issue here. National insures \$88,245,000 in current outstanding principal balance of Unlimited Tax Bonds.

16. Plaintiff Assured Guaranty Municipal Corp. is a New York corporation with its principal place of business at 31 West 52nd Street, New York, New York 10019. Assured is a monoline insurer that provides financial guarantees to the U.S. public finance market. Assured and its affiliates insure or reinsure approximately \$2.1 billion in net principal amount of outstanding bonds issued by the City, including water supply system bonds, sewage disposal system bonds, and the Unlimited Tax Bonds. The Unlimited Tax Bonds are the only bonds insured by Assured that are at issue here. Assured insures \$168,855,000 in current outstanding principal balance of Unlimited Tax Bonds. “Assured” herein shall



include Assured and any of its affiliates that insure or reinsure Unlimited Tax Bonds.

17. Defendant City is a home rule city under Act 279 of 1909, as amended, the Home Rule City Act, MCL § 117.1, *et seq.* (“Act 279,” attached hereto as Exhibit F). The City is a municipality that commenced a chapter 9 proceeding in the United States Bankruptcy Court for the Eastern District of Michigan on July 18, 2013.

18. Defendant Kevyn D. Orr is the Emergency Manager for the City (the “Emergency Manager”), as authorized by Public Act 436 of 2012 of the State of Michigan, also known as the Local Financial Stability and Choice Act, MCL §§ 141.1541-141.1575 (“Act 436,” attached hereto as Exhibit G). Mr. Orr’s appointment to the position of Emergency Manager became effective on March 28, 2013.

19. Defendant John Naglick is the Finance Director of the City (the “Finance Director”), having served in that position since October 7, 2013.

20. Defendant Michael Jamison is the Deputy Finance Director of the City (the “Deputy Finance Director”), having served in that position since August 2012.

21. Defendant Cheryl Johnson is the former Finance Director and current Treasurer of the City (the “Treasurer,” and collectively with the Emergency

Manager, Finance Director, and Deputy Finance Director, the “Individual Defendants”).

22. Joinder of all defendants is proper under Rule 20 of the Federal Rules of Civil Procedure, made applicable hereto by Bankruptcy Rule 7020.

### **JURISDICTION AND VENUE**

23. This Court has jurisdiction over this adversary proceeding pursuant to 28 U.S.C. § 1334(b) and the Standing Order of Reference to the Bankruptcy Court in the Eastern District of Michigan, E.D. Mich. L.R. 83.50(a), pursuant to 28 U.S.C. § 157(a). Subject matter jurisdiction exists pursuant to 28 U.S.C. § 157(b) as a case under Title 11 of the United States Code (the “Bankruptcy Code” or “Title 11”) and a core proceeding arising under Title 11, or arising in a case under Title 11 in accordance with 28 U.S.C. § 157(b)(2).

24. As described in greater detail herein, there is an actual case and controversy under 28 U.S.C. § 2201(a).

25. Venue of the case is proper in this District pursuant to 28 U.S.C. §§ 1408 and 1409.

### **GENERAL ALLEGATIONS**

#### **I. The City’s Unlimited Tax Bonds**

26. According to the City’s Proposal to Creditors, dated June 14, 2013 (the “Prepetition Proposal,” attached hereto as Exhibit H), the City estimates that,

as of the close of Fiscal Year 2013 (*i.e.*, June 30, 2013), it had \$369.1 million in outstanding principal amount of Unlimited Tax Bonds (excluding \$100 million of bonds payable first by a second lien on distributable state aid). National and Assured together insure \$257,100,000 in principal of the City's Unlimited Tax Bonds, maturing through April 1, 2028.

27. As bond insurers, National and Assured are obligated to pay to owners of the Unlimited Tax Bonds the full principal and interest when due as required by their respective bond insurance policies to the extent the City does not discharge its obligations under the insured Unlimited Tax Bonds. Under relevant provisions of the applicable bond documents, bond insurance policies, and applicable law, to the extent National and Assured make payments under their respective policies, they are subrogated to the rights of the Bondholders and effectively step into the shoes of such Bondholders.

## **II. The National-Insured Bonds**

28. Pursuant to the April 6, 2001 Resolution, the June 13, 2001 Supplemental Resolution, and a sale order issued by the City's then finance director on August 1, 2001 (the "2001 Sale Order"), the City issued General Obligation Bonds (Unlimited Tax) Series 2001-A(1) (the "2001-A(1) Bonds"), General Obligation Bonds (Unlimited Tax) Series 2001-A(2) (the "2001-A(2) Bonds"), and General Obligation Refunding Bonds (Unlimited Tax), Series 2001-

B (the “2001-B Bonds,” and, collectively with the 2001-A(1) and 2001-A(2) Bonds, the “2001 Bonds”).

29. Pursuant to the July 24, 2002 Resolution and a sale order issued by the City’s then finance director on August 2, 2002 (the “2002 Sale Order”), the City issued General Obligation Bonds (Unlimited Tax), Series 2002 (the “2002 Bonds,” and, collectively with the 2001 Bonds, the “National Bonds,” attached hereto as Exhibit I).

30. National issued Financial Guaranty Insurance Policies (the “National Policies,” attached hereto as Exhibit J) insuring the City’s payment obligations under the National Bonds. National issued Financial Guaranty Insurance Policy numbers 35874, 35875, and 35876, effective August 8, 2001, insuring the City’s payment obligations under the 2001-A(1) Bonds, the 2001-A(2) Bonds, and the 2001-B Bonds, respectively. National issued Financial Guaranty Insurance Policy number 38697, effective August 8, 2002, insuring the City’s payment obligations under the 2002 Bonds.

### **III. The Assured-Insured Bonds**

31. Pursuant to the March 3, 1999 Resolution and a sale order issued by the then finance director on April 1, 1999 (the “1999 Sale Order”), the City issued General Obligation Bonds (Unlimited Tax) Series 1999-A (the “1999 Bonds”).

32. Pursuant to the July 6, 2005 Resolution and a sale order issued by the then finance director on December 5, 2005 (the “2005 Sale Order”), the City issued General Obligation Bonds (Unlimited Tax) Series 2005-B (the “2005-B Bonds”) and General Obligation Refunding Bonds (Unlimited Tax) Series 2005-C (the “2005-C Bonds”) and, collectively with the 2005-B Bonds, the “2005 Bonds”).

33. Pursuant to the November 17, 2006 Resolution and a sale order issued by the then finance director on May 30, 2008 (the “2008 Sale Order” and, collectively with the 1999 Sale Order, 2001 Sale Order, 2002 Sale Order, and 2005 Sale Order, the “Sale Orders,” attached hereto as Exhibit K), the City issued General Obligation Bonds (Unlimited Tax) Series 2008-A (the “2008-A Bonds”), General Obligation Refunding Bonds (Unlimited Tax) Series 2008-B(1) (the “2008-B(1) Bonds”) and General Obligation Refunding Bonds (Unlimited Tax) Series 2008-B(2) (the “2008-B(2) Bonds”) and, collectively with the 2008-A Bonds, 2008-B(1) Bonds, the “2008 Bonds”; and the 2008 Bonds collectively with the 1999 Bonds and 2005 Bonds, the “Assured Bonds,” attached hereto as Exhibit L).

34. Assured, under its former name Financial Security Assurance Inc., and its affiliate, Assured Guaranty Corp., issued municipal bond insurance policies (the “Assured Policies,” attached hereto as Exhibit M) insuring the City’s payment obligations under the Assured Bonds. Assured issued Municipal Bond Insurance

Policy number 25071-N, effective April 13, 1999, insuring the City's payment obligations under certain 1999 Bonds. Assured issued Municipal Bond Insurance Policy numbers 206130-N and 206129-N, effective December 13, 2005, insuring the City's payment obligations under the 2005-B Bonds and the 2005-C Bonds, respectively. Assured Guaranty Corp. issued Financial Guaranty Insurance Policy number D-2008-477, effective June 9, 2008, insuring the City's payment obligations under the 2008 Bonds.

#### **IV. The City is Statutorily Required to Levy, Collect, and Deposit the Restricted Funds in Segregated Debt Retirement Funds**

35. The City's issuance of the Unlimited Tax Bonds is authorized and governed by Act 34, Act 189, Act 279, and the Michigan Constitution. Under Act 34, municipal securities such as the Unlimited Tax Bonds may be "payable from or secured by" any of the following: (i) *ad valorem* real and personal property taxes, (ii) special assessments, (iii) the unlimited full faith and credit pledge of the municipality, and (iv) other sources of revenue described in Act 34 for debt or securities authorized by Act 34. MCL § 141.2103(l); *see also* MCL §§ 141.2315(1)(c)(i), (2) (authorizing the City to issue municipal securities "payable from . . . [t]axes and other revenues of the municipality" and referring to such municipal securities as "additionally secured").

36. Michigan has adopted a separate statute, the Unlimited Tax Election Act, specifically to regulate the imposition of the Unlimited Tax Levy and the use

of taxes collected under that levy for the payment of Unlimited Tax Bonds. MCL § 141.161 *et seq.* The Unlimited Tax Election Act provides that upon voter approval the City “may make 1 or more binding unlimited tax pledges for the payment of 1 or more tax obligations referred to in the ballot, . . . . [h]owever, the tax which may be levied shall not be excess of a rate or amount sufficient for payment of the obligations.” MCL § 141.164(3). “Unlimited tax pledges” secure the payment of the Unlimited Tax Bonds. *See* MCL § 141.162(d); *see also* MCL § 141.164(1) (describing “tax obligations . . . secured by unlimited tax pledges of the public corporation if approved by its electors”).

37. The City has the authority to impose the Unlimited Tax Levy annually only so long as the Unlimited Tax Bonds are outstanding. *See* MCL §§ 141.2701, 141.164(3).

38. In addition, the Uniform Budgeting and Accounting Act (attached hereto as Exhibit N) requires the City’s tax legislation to specify the purpose for each component of the *ad valorem* tax levy, thereby dictating that Unlimited Tax Bond debt service must be a specific and separate line item in each budget and tax bill. MCL § 141.421 *et seq.*

39. At the time the Unlimited Tax Bonds were issued, the City had already reached the applicable maximum constitutional, statutory, or charter tax rate for *ad valorem* taxes levied for purposes unrelated to the payment of debt

service for the Unlimited Tax Bonds. Because voters approved the Unlimited Tax Bonds, however, the otherwise applicable maximum limitations on millage do not apply to the Unlimited Tax Levy. Accordingly, the City has relied on this special millage rate exception to levy a separate stream of *ad valorem* taxes in excess of the otherwise applicable constitutional, statutory, or charter tax rate limitations for the sole purpose of repaying the Unlimited Tax Bonds.

40. The Restricted Funds are *ad valorem* taxes specifically levied and collected to repay the Unlimited Tax Bonds,<sup>2</sup> which were issued to finance certain specific City projects and systems, including but not limited to projects relating to neighborhood/economic development, recreation, zoo and cultural facilities improvements, police and fire buildings and sites and other public safety facilities, public lighting system improvements, Detroit Institute of Arts improvements, Department of Public Works improvements, funding of the City's risk management pool, and public health facilities improvements. The specific projects are described and voted upon in the related bond referenda. The specific projects and the amounts of financing for each project are also described in, among other

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<sup>2</sup> Certain series of Unlimited Tax Bonds are "refunding" bonds. That is, the proceeds of refunding Unlimited Tax Bonds were specifically designated to be, and were, used by the City to refinance (*i.e.*, refund or defease) other Unlimited Tax Bonds that financed capital projects. Under Act 34, the Restricted Funds originally pledged as security to repay the refunded or defeased Unlimited Tax Bonds are pledged as security to repay the refunding Unlimited Tax Bonds.



City documents, the Resolutions, and the official statements the City prepared in connection with the sale and issuance of the Unlimited Tax Bonds.

41. Michigan law and the Resolutions provide strict controls over and limitations upon use of the *ad valorem* taxes levied and collected to secure the repayment of the Unlimited Tax Bonds. *See, e.g.*, MCL §§ 141.2701, 141.2705; Resolutions § 301(a).

42. Section 701(1)(a) of Act 34 requires the City to include the following in the amount of *ad valorem* taxes levied each year: “An amount such that the estimated collections will be sufficient to promptly pay, when due, the interest on [the Unlimited Tax Bonds] and the portion of the principal falling due whether by maturity or by mandatory redemption before the time of the following year’s tax collection.” MCL § 141.2701(1)(a). In addition, Section 701(3) of Act 34 requires that the City “levy the full amount of taxes required . . . for the payment of [the Unlimited Tax Bonds] without limitation as to rate or amount and in addition to other taxes that the municipality may be authorized to levy.” MCL § 141.2701(3).

43. Act 34 then requires that the *ad valorem* taxes be deposited in segregated Debt Retirement Funds as they are collected: “As taxes are collected, there shall be set aside that portion of the collections that is allocable to the payment of the principal and interest on [the Unlimited Tax Bonds]. The portion set aside shall be divided pro rata among the various sinking funds and debt

retirement funds in accordance with the amount levied for that purpose.” MCL § 141.2701(6).

44. Section 701(1)(d)(i) of Act 34 further provides that the taxes specifically collected and pledged for repayment of the Unlimited Tax Bonds must be deposited in the applicable Debt Retirement Funds and used for no purpose other than to pay the debt service on the Unlimited Tax Bonds. As relevant here, Section 701(1)(d)(i) requires that the proceeds of the tax levy be “[d]eposit[ed] in the debt retirement fund established for the [Unlimited Tax Bonds] and used to pay debt service charges or obligations on [the Unlimited Tax Bonds].” MCL § 141.2701(1)(d)(i).

45. Section 705 of Act 34 states, in relevant part, that each debt retirement fund “shall be accounted for separately.” Section 705 further provides that the “debt retirement funds . . . shall be used only to retire the municipal securities of the municipality for which the debt retirement fund was created” and that they cannot be used for other purposes unless and until those municipal securities have been retired. MCL § 141.2705.

46. The Resolutions require that the *ad valorem* taxes levied under the Unlimited Tax Levy are pledged as security for the timely payment of principal and interest on the Unlimited Tax Bonds when due. Section 301(a) of the Resolutions states:

The City *pledges to pay the principal of and the interest on the [b]onds from the proceeds of an annual levy of ad valorem taxes on all taxable property in the City without limitation as to the rate or amount for the payment thereof.*

Resolutions § 301(a) (emphasis added). By its terms, Section 301 of the Resolutions creates an irrevocable pledge of the Restricted Funds as security for the repayment of the Unlimited Tax Bonds. Also included as security for the Unlimited Tax Bonds are “the unlimited tax, full faith, credit and resources of the City.” *Id.*

47. The Resolutions characterize the Unlimited Tax Bonds as “secured.” *See, e.g.*, July 24, 2002 Resolution §§ 202, 307, 309, 701, 1002, 1004.

48. Under Section 701 of the Resolutions, the City may not unilaterally diminish or adversely affect the security of the Bonds. *See* Resolutions § 701.

49. In addition, the proceeds of all taxes levied to repay the Unlimited Tax Bonds “shall be placed in the Debt Retirement Fund[s] and held in trust by the Paying Agent.” Resolutions § 502. So long as the principal of and interest on the Unlimited Tax Bonds remain unpaid, such amounts shall be used *only* to pay principal and interest, and “no moneys shall be withdrawn from the Debt Retirement Fund[s] *except* to pay such principal and interest.” *Id.* (emphasis added). Section 601 of the Resolutions and Section 401 of the Sale Orders provide that U.S. Bank National Association shall serve as the Paying Agent for the Unlimited Tax Bonds.

50. The limitations set forth under Michigan law and the Resolutions were expressly recognized in the State of Michigan Attorney General Opinion, dated February 19, 1982 (the “Attorney General Opinion,” attached hereto as Exhibit O), which states that the taxes levied for the payment of principal and interest on bonds must “be placed in a segregated account” and “may only be used to pay principal and interest on the bonds for which the millage was levied while the bonds are outstanding.” 1981-1982 Mich. Op. Att’y Gen. 575 (1982).

51. Accordingly, the City lacks any equitable or beneficial property interest in the Restricted Funds, which consist of the *ad valorem* taxes specifically authorized, levied, collected, and pledged to secure the repayment of the Unlimited Tax Bonds. “But for” voter approval, the City could not levy and collect these *ad valorem* taxes. Further, the City is prohibited by law from collecting and using these *ad valorem* taxes except to pay principal of and interest on the Unlimited Tax Bonds. Nothing in chapter 9 or federal bankruptcy law allows the City to disregard state-law restrictions imposed on the Restricted Funds and use such funds for non-authorized purposes.

**V. The City Historically Has Administered the Unlimited Tax Bonds Consistent with Michigan Law.**

52. In a series of bond referenda held between 1978 to 2004, voters provided the City with the authority required by Michigan law to issue the Unlimited Tax Bonds by giving their consent to unlimited *ad valorem* taxation

solely for the purpose of repaying the Unlimited Tax Bonds in exchange for the financing of capital improvement projects to benefit voters. Voter ballots for proposed bond referenda include the estimated first-year millage, the estimated millage over the Unlimited Tax Bonds' life, and the specific capital improvement projects to be financed by the Unlimited Tax Bonds. *See* App. A; MCL § 211.24f (establishing ballot requirements for proposed bond referenda).

53. The proceeds (net of issuance costs) from the outstanding series of Unlimited Tax Bonds were to be used only to fund or finance specific capital improvement projects as described in paragraph 40 *supra*. Upon information and belief, no proceeds from the outstanding series of Unlimited Tax Bonds were used for the purpose of paying the City's operating expenses or for general purposes.

54. When issuing the Unlimited Tax Bonds, the City represented in its offering memoranda for each series of Unlimited Tax Bonds that: "The City is authorized and required by law to levy and collect *ad valorem* taxes upon all taxable property in the City, without limitation as to rate or amount, to pay principal of and interest on the Bonds when due." *See, e.g.,* City of Detroit, Official Statement for General Obligation Bonds (Unlimited Tax) Series 2008-A, 2008-B(1), and 2008-B(2), and (Limited Tax) Series 2008-A(1) and 2008-A(2), at 2 ("2008 Official Statement," attached hereto as Exhibit P).

55. The City has stated that voter approval “is required in order to levy taxes in excess of the City’s general operating limit for payment of debt service.” City of Detroit, Proposed Capital Agenda for Fiscal Years 2005-06 to 2009-10, at 14 (attached hereto as Exhibit Q).

56. For each fiscal year since the issuance of the outstanding Unlimited Tax Bonds, the City, through its annual budget approval process, sets the annual millage rate for the Unlimited Tax Levy such that available money in the City’s Debt Retirement Funds is sufficient to fund the debt service for the Unlimited Tax Bonds for the year. The annual budget also shows the amount of millage expected to be collected under the Unlimited Tax Levy. The City annually adjusts the Unlimited Tax Levy’s millage rate because of, among other reasons, changes in the City’s assessment of the real property values, changes in debt service amounts, changes in properties exempt from *ad valorem* taxation, and changes in prior years’ collection rates.

57. The City annually sends taxpayers a summer *ad valorem* tax bill, which reflects the millage for the Unlimited Tax Levy as a separate line item described as “Debt Service.” There is also a separate line reflecting millage for City “General City Operating.” The City also uses the summer bill to levy *ad valorem* tax millage on behalf of other taxing authorities, such as the State of Michigan, Detroit Public School System, and County of Wayne.

58. The City's property taxes from the summer billing are due to the City on July 1 of each year and payable in full without penalty by August 31. Taxpayers may also pay in installments without penalty if they pay one-half of their taxes by August 15 with the balance paid by January 15. Most taxpayers choose to pay their *ad valorem* taxes in semi-annual installments. Consequently, the majority of *ad valorem* taxes that the City collects annually are paid in the months of August and January.

59. Among the funds the City has established to manage finances for its various activities, the City maintains a separate fund, known as the Debt Service Fund. The City uses the Debt Service Fund to account for the *ad valorem* tax receipts collected under the Unlimited Tax Levy and for the payment of debt service for the Unlimited Tax Bonds. *See, e.g.,* City of Detroit, Audited Comprehensive Annual Financial Report for the Fiscal Year Ended June 30, 2012, at 150 (the "FY 2012 CAFR," attached hereto as Exhibit R). The Debt Service Fund is a Debt Retirement Fund required by Act 34, and is described by the City as a "separate fund for debt retirement moneys" required "by State law." City of Detroit, 2008 Official Statement, at A-33.

60. The City has represented that the City Treasurer deposits *ad valorem* tax proceeds into the Debt Service Fund: "All City property taxes are collected by

the Treasurer and deposited in the appropriate funds according to the proper distribution percentage.” *See, e.g.*, 2008 Official Statement at A-33.

61. The City’s CAFRs confirm that the City’s accounting similarly reflects the segregation of *ad valorem* taxes collected under the Unlimited Tax Levy, reporting that the millage for the City’s general operations and millage for the Unlimited Tax Levy “are recognized in the respective General Fund and Debt Service Fund financial statements as tax revenue.” *See, e.g.*, FY 2012 CAFR at 75.

62. In the FY 2012 CAFR, the City reported that the Debt Service Fund had a balance of \$4,561,750 at the beginning of the fiscal year and an ending balance of \$6,314,687. FY 2012 CAFR at 174.

63. Disbursements from the Debt Service Fund are used to pay debt service owed on Unlimited Tax Bonds as principal and interest payments become due. The City has stated that Unlimited Tax Bonds “are repaid from a specific source[,] the Debt Service property tax levy.” City of Detroit, Proposed Capital Agenda for Fiscal Years 2013-14 to 2017-18, at 6 (attached hereto as Exhibit S).

64. The Paying Agent holds the Restricted Funds in trust in individual Debt Retirement Funds for each series of Unlimited Tax Bonds<sup>3</sup> and, from those accounts, disburses the debt service payments to holders of the Unlimited Tax

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<sup>3</sup> The individual Debt Retirement Funds consist of financial accounts that the City has established with Paying Agents to pay debt service owed for individual series of Unlimited Tax Bonds.



Bonds on the principal and interest payment dates. The City's Resolutions authorize the express trusts established with the Paying Agent and require that "so long as the principal of or interest on the Bonds shall remain unpaid, no moneys shall be withdrawn from the Debt Retirement Fund[s] except to pay such principal and interest." Resolutions § 502.

## **VI. Individual Defendants Have Nondiscretionary Duties Under Act 34**

65. Based on the City's representations, and the duties and responsibilities of the Emergency Manager, the Finance Director, the Deputy Finance Director, and the Treasurer, the Individual Defendants have failed to perform their duties under Act 34.<sup>4</sup>

66. Act 436 establishes the Emergency Manager as an officer whose duties include ensuring the City's compliance with Act 34's procedures for repayment of Unlimited Tax Bonds, including the segregation of Restricted Funds.

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<sup>4</sup> Act 34 provides that "[a]n officer who willfully fails to perform the duties required by [Section 701] is personally liable to the municipality or to a holder of a municipal security for loss or damage arising from his or her failure." MCL § 141.2701(7). Upon information and belief, the failures of Messrs. Orr, Naglick, and Jamison and Ms. Johnson to perform their duties with respect to Section 701 are the result of their respective intentional decisions, actions, and omissions with the intent to harm Bondholders and Plaintiffs. As a direct result of each of the Individual Defendants' failures to perform their respective duties pursuant to Act 34, Plaintiffs have been harmed. Notwithstanding the foregoing, the only relief that Plaintiffs currently seek herein against the Individual Defendants is declaratory relief that will bind the Individual Defendants in their official capacities to ensure compliance by the City and its pertinent officials with the dictates of Michigan law and the United States Constitution.

Act 436 requires the Emergency Manager to develop a written financial and operating plan for the City that provides for “[t]he payment in full of the scheduled debt service requirements on all bonds, notes, and municipal securities of the local government, contract obligations in anticipation of which bonds, notes, and municipal securities are issued, and all other uncontested legal obligations.” MCL § 141.1551(1)(b). To effectuate this mandate, it is within the Emergency Manager’s powers to “[r]eceive and disburse on behalf of the local government all . . . local funds earmarked for the local government. These funds may include, but are not limited to, funds for . . . retirement of debt.” MCL § 141.1552(1)(c).

67. On July 10, 2013, eight days before the City filed its chapter 9 petition, Mr. Orr issued Emergency Manager Order No. 12 (“EM Order No. 12,” attached hereto as Exhibit T), which established the City’s legal operating budget for Fiscal Year 2013-14. Order No. 12 required that the City’s Fiscal Year 2014 budget conform to the City’s Prepetition Proposal, which provided for the collection of millage under the Unlimited Tax Levy, but failed to allocate the proceeds to fund debt service for the Unlimited Tax Bonds due in Fiscal Year 2013-14. Thus, contrary to Acts 34 and 436, Mr. Orr’s financial and operating plan, as adopted in the City’s operating budget, (i) provides for the continued levy, collection, and unlawful diversion of the Restricted Funds for purposes other than

retirement of the Unlimited Tax Bonds and (ii) fails to provide for the payment of the semi-annual debt service due for the Unlimited Tax Bonds.

68. Mr. Orr has also authorized the City to divert more than \$95 million appropriated for debt payments on other bond obligations to pay more than a dozen law firms and consultants retained to assist the City with its restructuring.

69. Mr. Orr's conduct exceeded the scope of his executive authority under Act 436 by authorizing and implementing a pre-petition financial and operating plan that unlawfully diverted, and continues to divert, funds in violation of Michigan law and failed to provide for the full payment of debt service on the Unlimited Tax Bonds.

70. The City's Charter establishes the Finance Director as an officer who must perform the duties required by Act 34 with respect to the Restricted Funds. The nondiscretionary duties of the Finance Director under the City's Charter and City Code require Mr. Naglick as the Finance Director, and required Ms. Johnson as former Finance Director, to:

- a. "secure and maintain compliance *with all laws* pertaining to financial controls for the protection of public funds";
- b. "direct and coordinate the financial activities of the accounts division, the assessments division, the treasury, and the purchasing division";
- c. oversee and manage the Treasurer, who "serves at the pleasure of the Finance Director"; and

d. issue “a document *authorizing or requiring . . . payments*” to be disbursed by the Treasurer that “*specif[ies] the particular fund or agency out of which it is payable* and [is] accompanied by a check register indicating the names of the payees.”

City Charter §§ 6-302, 6-305; City Code § 18-1-3 (emphasis added).

71. The City’s Charter establishes the Deputy Finance Director as an officer who must perform the duties required by Act 34 with respect to the Restricted Funds. Mr. Jamison as Deputy Finance Director has the same nondiscretionary duties as the Finance Director under the City Charter. The City Charter requires that the “Deputy in each department of the executive branch shall, under the Director’s supervision, during the director’s absence or disability, or while the director’s position is vacant, exercise all the powers and perform all the duties of the director to the full extent permitted by law.” City Charter § 5-107.

72. The City’s Charter and City Code establish the Treasurer as an officer who must perform the duties required by Act 34 with respect to the Restricted Funds. The nondiscretionary duties of the Treasurer under the City’s Charter and City Code require Ms. Johnson as Treasurer to:

- a. “Collect all moneys of the city and receive from other officers and employees all moneys of the city collected by them”;
- b. “Have custody of all moneys, funds and securities of the city, keep accounts of them and deposit them *as directed by law or ordinance*”;

- c. “Disburse all city funds *in accordance with law*, this Charter or ordinance”;
- d. “Except as otherwise provided by this Charter or ordinance, have such powers and immunities for the collection of taxes *as provided by law*”;
- e. “[D]eposit, daily, his entire receipts from all sources and all money and checks on hand to the credit of the city in such banks as may be designated by the city council as the depository of the funds of the city”;
- f. Designate an account in which certain banks shall deposit all such tax money that the banks have accepted as deposits from taxpayers to the credit of the City for payment of “real and personal property taxes that are levied by the City each fiscal year”;
- g. Receive from banks collecting real and personal property tax payments “all duplicate paid tax bills for which the[] [banks] have received payment, together with a duplicate deposit slip for the full amount of taxes paid on the preceding banking business day” and “a list showing the tax bill item number appearing on each paid tax bill and the amount paid for which such tax receipt was issued”;
- h. “[P]ay out no money except by his check on the banks specified by the city council. Such check shall be issued only upon the issuance by the finance director of a document authorizing or requiring the payment of the sum specified therein. Such document shall specify the particular fund or agency out of which it is payable and be accompanied by a check register indicating the names of the payees”; and
- i. “[T]ransmit by mail, unless otherwise directed by the owner, to each owner of registered bonds of the city, at his last known post office address, a draft or check payable in New York at par for the amount of interest due thereon, which draft

or check *shall be mailed at least twenty-four (24) hours prior to the maturity of the interest.*”

City Charter § 6-305; City Code §§ 18-1-2 to -1-3, 18-7-8, 18-9-71, 18-9-74 to -9-75 (emphasis added).

73. Notwithstanding their respective legal duties, Messrs. Orr, Naglick, and Jamison and Ms. Johnson each failed (i) to levy *ad valorem* taxes for the payment of debt service for the Unlimited Tax Bonds, insofar as the City has represented to taxpayers that the millage it is collecting is for the repayment of the Unlimited Tax Bonds without having used the tax proceeds for that purpose, and (ii) to set aside and pay the Restricted Funds into the appropriate Debt Retirement Funds in accordance with the amounts levied for the payment of debt service on the Unlimited Tax Bonds.

74. In addition, Messrs. Orr, Naglick, and Jamison and Ms. Johnson each intended to divert the Restricted Funds by failing to follow Act 34’s order of priority for the restricted use of the Restricted Funds, beginning with “the retirement of all municipal securities payable from [a debt retirement] fund.” MCL § 141.2704(5).

## **VII. Plaintiffs Have Property Interests in the Restricted Funds**

75. The Bondholders and Plaintiffs have equitable and beneficial property interests in the Restricted Funds. Further, the Restricted Funds are impressed with

a statutory lien as defined in section 11 U.S.C. § 101(53) and, in addition, constitute “special revenues” as defined in 11 U.S.C. § 902(2)(E).

**A. Plaintiffs Have Equitable and Beneficial Property Interests in the Restricted Funds**

76. By authorizing the issuance of the Unlimited Tax Bonds, the City’s taxpayers consented to the Unlimited Tax Levy for the sole purpose of repaying the Unlimited Tax Bonds. The taxpayers thus disclaimed any title to, possession of, or control over the proceeds collected under the Unlimited Tax Levy in exchange for the capital improvements financed by the Unlimited Tax Bonds.

77. The City is merely a conduit for transferring proceeds of *ad valorem* taxes collected under the Unlimited Tax Levy from taxpayers to Bondholders.

78. Although Michigan law requires the City to collect and segregate the Restricted Funds, no provision of Michigan law vests the City with any equitable or beneficial property interest in the Restricted Funds.

79. Any control the City exercises by segregating the Restricted Funds in Debt Retirement Funds and transferring the Restricted Funds to be held in trust by the Paying Agent is for the exclusive purpose of paying debt service for the Unlimited Tax Bonds and thus is for the benefit of the Bondholders (and Plaintiffs as the Bondholders’ subrogees). Accordingly, the Bondholders hold equitable and beneficial property interests in the Restricted Funds.

**B. Plaintiffs Have a Statutory Lien on the Restricted Funds**

80. Under Michigan law, voter approval for the Unlimited Tax Bonds authorizes the City to make a binding unlimited tax pledge, which is an “undertaking by a public corporation *to secure and pay* a tax obligation *from ad valorem taxes to be levied on all taxable property* within the boundaries of the public corporation without limitation as to rate or amount and in addition to other taxes which the public corporation may be authorized to levy.” MCL § 141.162(d) (emphasis added).

81. In passing the authorizing Resolutions for the respective Unlimited Tax Bonds, which are valid legislative acts of the City Council, the City “pledge[d] to pay the principal of and interest on the Bonds from the proceeds of” the Unlimited Tax Levy. Resolutions § 301. This pledge constitutes a binding unlimited tax pledge as defined by Michigan law. MCL §§ 141.162(d), 141.164(3).

82. Accordingly, a statutory lien exists on the Restricted Funds within the meaning of 11 U.S.C. § 101(53) (defining a “statutory lien” as arising “by force of a statute . . . whether or not such interest or lien is made fully effective by statute”). The City explicitly recognized the creation of a statutory lien on the Restricted Funds by pledging the Restricted Funds solely to the repayment of the Unlimited



Tax Bonds and characterizing the pledge as the “lien of this Resolution for the benefit of such Bonds.” Resolutions § 801.

**C. Plaintiffs Have a Lien on Special Revenues, Which are the Restricted Funds**

83. As noted above, the Bondholders (and Plaintiffs as the Bondholders’ subrogees) have a statutory lien on the Restricted Funds. Additionally, or in the alternative, they have a lien on the Restricted Funds as a result of the City’s Resolutions and Sales Orders, which constitute prepetition agreements between the City, Bondholders, and Plaintiffs, and create or provide for a security interest for the Unlimited Tax Bonds. *See* 11 U.S.C. § 101(37) (defining a “lien” as a “charge against interest in property to secure payment of the debt or performance of an obligation”).

84. The Restricted Funds are special revenues within the meaning of 11 U.S.C. § 902(2)(E) (defining special revenues as “taxes specifically levied to finance one or more projects or systems”). These *ad valorem* taxes were exclusively levied under a special tax levy to repay Unlimited Tax Bonds issued to finance capital improvements and are distinguishable and separate from *ad valorem* taxes that the City levies for its general or operating purposes. *See, e.g.,* MCL § 211.24e(1)(i) (defining “operating purposes” as “all purposes for which ad valorem property taxes are levied by the taxing unit other than the levy of ad valorem property taxes . . . to pay principal and interest due on a bond or note if

and to the extent the ad valorem taxes levied for this purpose are in addition to charter or statutory limitations, as authorized by [Act 34]”). Upon information and belief, no Unlimited Tax Bond proceeds were used for the purpose of paying the City’s operating expenses or for general purposes.

85. Furthermore, state law requires that these specific *ad valorem* taxes not be used for any purpose other than paying the Bondholders. Accordingly, the pledged *ad valorem* taxes are wholly dedicated to repayment of outstanding Unlimited Tax Bonds and not otherwise available to fund distributions to creditors under a plan of adjustment or for any other purpose.

86. Because the Restricted Funds are special revenues “pledged . . . to payment of indebtedness secured by such revenues,” the Restricted Funds are not subject to the automatic stay by 11 U.S.C. §§ 362 and 922(a) pursuant to 11 U.S.C. § 922(d) and must be applied by the City in a manner consistent with 11 U.S.C. § 928 (providing that “special revenues acquired by the debtor after the commencement of the [bankruptcy proceeding] shall remain subject to any lien resulting from any security agreement entered into by the debtor before the commencement of the [bankruptcy proceeding]”).

### **VIII. The Prepetition Proposal; National’s Demand Letter; and Proposed Postpetition Financing**

87. In both the City’s FY 2102 CAFR, independently audited by KPMG LLP pursuant to Michigan law, and the City’s Ten-Year Plan, dated June 26, 2013

(the “Ten-Year Plan,” attached hereto as Exhibit U), the City reports that in Fiscal Year 2011-12 it levied and collected *ad valorem* taxes in an amount sufficient to pay the debt service owed on the Unlimited Tax Bonds, excluding bonds payable first from distributable state aid.

88. For Fiscal Year 2013-14, the City’s Ten-Year Plan forecasts that the City will levy and collect *ad valorem* taxes in an amount sufficient to pay the Unlimited Tax Bonds. In the current fiscal year, the City budgeted, levied, and has been collecting *ad valorem* taxes using the Unlimited Tax Levy in an amount sufficient to pay debt service on the Unlimited Tax Bonds.

89. In its Prepetition Proposal, the City stated that it would continue to collect the Restricted Funds, but use the Restricted Funds for purposes other than paying principal of and interest on the Unlimited Tax Bonds. The City operates under a Fiscal Year 2014 budget that has been conformed with the City’s Prepetition Proposal pursuant to EM Order No. 12. Consequently, the City’s budget requires the City to collect the Restricted Funds and use those taxes for purposes other than paying principal of and interest on the Unlimited Tax Bonds—conduct that violates Michigan law and the Fifth and Fourteenth Amendments to the United States Constitution.

90. On July 12, 2013, National wrote the City a letter (the “Demand Letter,” attached hereto as Exhibit V) demanding, among other things, that the City

demonstrate by July 18, 2013 that the City was segregating the *ad valorem* taxes and that it had not used such taxes for any purposes other than to pay principal of and interest on the Unlimited Tax Bonds. The City provided only limited information in response to the Demand Letter, and failed to provide National any assurance that the Restricted Funds would be segregated and used in compliance with Michigan law.

91. On October 1, 2013, the City failed to make a payment due on the Unlimited Tax Bonds in the amount of almost \$9.4 million, and the Paying Agent made claims under the respective policies for a portion of such amount, which were duly paid by National and Assured. Thus, National and Assured are subrogated to the rights of the Bondholders and hold direct claims against the City in such amount.

92. By using the Restricted Funds for purposes other than the repayment of the Unlimited Tax Bonds, the City has taken the Bondholders' and Plaintiffs' equitable and beneficial property interests. The City has not provided any compensation for this taking of private property.

93. On November 5, 2013, the City filed the Motion of the Debtor for a Final Order Pursuant to 11 U.S.C. §§ 105, 362, 364(c)(1), 364(c)(2), 364(e), 364(f), 503, 507(a)(2), 904, 921 and 922 (I) Approving Post-Petition Financing, (II) Granting Liens and Providing Superpriority Claim Status and (III) Modifying

Automatic Stay [Docket No. 1520] (the “Financing Motion”). The relief requested in the Financing Motion (if approved by this Court) would grant Barclays Capital, Inc. (“Barclays”) super-priority status, pursuant to Sections 364 (“Section 364”), 503, and 507 of the Bankruptcy Code, over administrative expenses, postpetition claims, and all prepetition unsecured claims.<sup>5</sup>

94. If the City, pursuant to its stated intention, continues to use the Restricted Funds for purposes other than the repayment of the Unlimited Tax Bonds, or grants any postpetition interest in the Restricted Funds to any creditor or any other person, the Bondholders’ and Plaintiffs’ property interests will continue to be impaired unjustly. The City has not offered to provide any compensation for such impairment.

95. The relief sought in this Complaint is ripe for adjudication by this Court because, among other reasons, (1) the City in its Prepetition Proposal indicated that it would not segregate the Restricted Funds as required by Michigan law and is operating under a budget that provides the same, (2) the City defaulted

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<sup>5</sup> The City’s proposed Order with respect to the Financing Motion provides that if Plaintiffs prevail in this adversary proceeding on one or more counts, Barclays would not have super-priority status over the Restricted Funds. Accordingly, at this time Plaintiffs are not seeking any declaratory relief concerning the City’s grant of super-priority status over the Restricted Funds as a violation of Plaintiffs’ rights, but reserve the right to do so. *See* Second Notice of Revised Proposed Order in Connection with Motion of the Debtor for a Final Order Pursuant to 11 U.S.C. §§ 105, 362, 364(c)(1), 364(c)(2), 364(e), 364(f), 503, 507(a)(2), 904, 921 and 922 (I) Approving Post-Petition Financing, (II) Granting Liens and Providing Superpriority Claim Status and (III) Modifying Automatic Stay [Docket No. 2177].

on its obligation to pay \$9.4 million in interest payments on the Unlimited Tax Bonds due on October 1, 2013 notwithstanding that it levied and collected sufficient *ad valorem* taxes to pay the Bondholders, (3) the City apparently intends to default on \$47.58 million in principal and interest payments due on April 1, 2014, and (4) the City has not segregated but rather has diverted (and apparently intends to continue to divert) the Restricted Funds.

### COUNT ONE

**Declaratory Judgment that the *Ad Valorem* Taxes Collected Under  
the Unlimited Tax Levy Are Restricted By Michigan Law and  
Cannot be Levied, Collected, or Used by the City  
Except to Repay the Unlimited Tax Bonds**

96. Plaintiffs hereby incorporate the preceding paragraphs as if fully set forth herein.

97. An actual, ripe, and justiciable controversy has arisen between the parties regarding whether the *ad valorem* taxes collected under the Unlimited Tax Levy are restricted by Michigan law, and cannot be levied, collected, or used by the City for any other purpose except to satisfy the City's payment obligations with respect to outstanding Unlimited Tax Bonds.

98. For the reasons stated herein, Plaintiffs are entitled to a declaratory judgment that under Michigan law the *ad valorem* taxes collected under the Unlimited Tax Levy are restricted and cannot be levied, collected, or used by the

City for any other purpose except to satisfy the City's payment obligations with respect to outstanding Unlimited Tax Bonds.

## **COUNT TWO**

### **Declaratory Judgment that the City Has No Equitable or Beneficial Property Interest in the Restricted Funds and Bondholders and Plaintiffs Have Equitable and Beneficial Property Interests in the Restricted Funds**

99. Plaintiffs hereby incorporate the preceding paragraphs as if fully set forth herein.

100. An actual, ripe, and justiciable controversy has arisen between the parties regarding Plaintiffs' equitable and beneficial property interests in the Restricted Funds.

101. Neither the City's taxpayers, nor the City, have any equitable or beneficial interests in the Restricted Funds. The City is a mere conduit for transferring the *ad valorem* taxes collected under the Unlimited Tax Levy from taxpayers to Bondholders (and Plaintiffs as the Bondholders' subrogees). The City's collection and segregation of the Restricted Funds is for the exclusive purpose of paying debt service for the Unlimited Bonds and thus is for the benefit of the Bondholders (and Plaintiffs as the Bondholders' subrogees).

102. For the reasons stated herein, Plaintiffs are entitled to a declaratory judgment that (i) the City is a conduit for the Restricted Funds and lacks any equitable or beneficial property interest in the Restricted Funds and (ii) the

Bondholders and Plaintiffs, as the Bondholders' subrogees, have equitable and beneficial property interests in the Restricted Funds.

### **COUNT THREE**

#### **Declaratory Judgment that the Unlimited Tax Bonds Are Secured by a Statutory Lien on the Restricted Funds**

103. Plaintiffs hereby incorporate the preceding paragraphs as if fully set forth herein.

104. An actual, ripe, and justiciable controversy has arisen between the parties regarding the validity, priority, and extent of Plaintiffs lien or other interests in the Restricted Funds.

105. The Bondholders and Plaintiffs have a statutory lien on the Restricted Funds within the meaning of 11 U.S.C. §§ 101(37) and (53) because, solely by force of Michigan law and the City's Resolutions, which are valid legislative acts of the City Council, the City's pledge of Restricted Funds constitutes a charge against or interest in the Restricted Funds to secure payment of the Unlimited Bonds. *See* 11 U.S.C. §§ 101(37), (53).

106. For the reasons stated herein, Plaintiffs are entitled to a declaratory judgment that the Unlimited Tax Bonds are secured by a statutory lien on the Restricted Funds.



## COUNT FOUR

### **Declaratory Judgment that Plaintiffs' Lien on the Restricted Funds is a Lien on Special Revenues**

107. Plaintiffs hereby incorporate the preceding paragraphs as if fully set forth herein.

108. An actual, ripe, and justiciable controversy has arisen between the parties regarding whether Plaintiffs' lien on the Restricted Funds constitutes a lien on special revenues within the meaning of 11 U.S.C. §§ 902(2)(E), 928.

109. The Bondholders and Plaintiffs have a lien on the Restricted Funds. This lien is a statutory lien arising from Michigan law and the City's Resolutions as described in paragraph 105 *supra*. Additionally, or in the alternative, the Bondholders and Plaintiffs have a lien on the Restricted Funds as a result of the City's Resolutions and Sales Orders, which constitute perpetuation security agreements between the City, Bondholders, and Plaintiffs and create or provide for a security interest for the Unlimited Tax Bonds.

110. The Restricted Funds constitute special revenues because they are pledged *ad valorem* taxes specifically levied and collected only to finance one or more capital projects and not to finance the general purposes of the City. *See* 11 U.S.C. § 902(2)(E) (defining special revenues as "taxes specifically levied to finance one or more projects or systems, excluding receipts from general property, sales, or income taxes (other than tax-increment financing) levied to finance the

general purposes of the debtor”); H.R. Rep. No. 100-1011, at 6 (1988) (explaining that § 902(2)(E) “define[s] special revenues to include the revenue derived . . . from a specific tax levy, where such revenues are meant to serve as security to the bondholders,” and identifying that Congress intended for § 902 to cover “pledged property tax revenues” that state law bars the debtor from “using . . . for any purpose other than paying the revenue bondholders”).

111. Under 11 U.S.C. § 922(d), the automatic stay does not operate as a stay of the application of the Restricted Funds to payment of the Unlimited Tax Bonds during the City’s chapter 9 case. More specifically, 11 U.S.C. § 922(d) “does not operate as a stay of application of pledged special revenues in a manner consistent with section 92[8] of this title to payment of indebtedness secured by such revenues.”

112. Under 11 U.S.C. § 928, any Restricted Funds acquired by the City after the commencement of its chapter 9 case shall remain subject to any lien on the Restricted Funds that existed before the commencement of the City’s chapter 9 case.

113. For the reasons stated herein, Plaintiffs are entitled to a declaratory judgment that the Restricted Funds are special revenues within the meaning of 11 U.S.C. § 902(2)(E) and must be applied in accordance with 11 U.S.C. §§ 922(d) and 928.

## COUNT FIVE

### **Declaratory Judgment that the City's Diversion of the Restricted Funds, Without Just Compensation to Plaintiffs, Is an Unlawful Taking Under the Fifth and Fourteenth Amendments to the United States Constitution**

114. Plaintiffs hereby incorporate the preceding paragraphs as if fully set forth herein.

115. An actual, ripe, and justiciable controversy has arisen between the parties regarding whether there has been an unlawful taking of Bondholders' and Plaintiffs' property under the Fifth and Fourteenth Amendments to the United States Constitution because of the City's use of the Restricted Funds for purposes other than repaying the Unlimited Tax Bonds.

116. The City has made clear to Plaintiffs that it will not segregate the Restricted Funds and has already used, and intends to continue to use, the Restricted Funds for purposes other than repayment of the Unlimited Tax Bonds.

117. The City may seek to grant postpetition interests in the Restricted Funds to creditors or other persons that would impair the Bondholders' and Plaintiffs' property interests in the Restricted Funds.

118. The City has taken and intends to continue to take these actions in derogation of Bondholders' and Plaintiffs' property interests without providing just compensation.

119. For the reasons stated herein, Plaintiffs are entitled to a declaratory judgment that (i) the City's use of the Restricted Funds for any purpose other than the repayment of the Unlimited Tax Bonds and (ii) any postpetition grant of interest in the Restricted Funds to any creditor or any other person, would impair the Bondholders' and Plaintiffs' property interests in the Restricted Funds and therefore would be unlawful takings of property without just compensation under the Fifth and Fourteenth Amendments to the United States Constitution.

### **COUNT SIX**

#### **Declaratory Judgment that Michigan Law Requires the Restricted Funds to be Segregated and Deposited into the Debt Retirement Funds and Not Commingled or Used for Purposes Other Than Repaying Bondholders**

120. Plaintiffs hereby incorporate the preceding paragraphs as if fully set forth herein.

121. An actual, ripe, and justiciable controversy has arisen between the parties regarding whether Michigan law requires Defendants to segregate the Restricted Funds and prohibits their diversion for purposes other than repayment of the Unlimited Tax Bonds.

122. Michigan law requires the Defendants to (i) impose the Unlimited Tax Levy *for* the payment of debt service for the Unlimited Tax Bonds, (ii) collect the *ad valorem* taxes levied to repay the Unlimited Tax Bonds and deposit such taxes

in segregated debt retirement funds, and (iii) use such taxes only to repay the outstanding Unlimited Tax Bonds and for no other purpose.

123. Defendants have made clear to Plaintiffs that they have not and will not segregate the Restricted Funds and have already used, and intend to continue to use, the Restricted Funds for purposes other than repayment of the Unlimited Tax Bonds, in contravention of Michigan law and in derogation of Plaintiffs' rights.

124. For the reasons stated herein, Plaintiffs are entitled to a declaratory judgment that, under Michigan law, as *ad valorem* taxes are collected under the Unlimited Tax Levy, the Restricted Funds must be (i) segregated and deposited, as allocable to each series of Unlimited Tax Bonds, into the related Debt Retirement Funds, and (ii) not commingled with other funds of the City or used for any purpose other than repaying the Bondholders (or Plaintiffs as the Bondholders' subrogees).

## REQUESTS FOR RELIEF

WHEREFORE, Plaintiffs respectfully request entry of a declaratory judgment:

- i. On Count One, declaring that, under Michigan law *ad valorem* taxes collected under the Unlimited Tax Levy are restricted by law and cannot be levied, collected, or used by the City for any other purpose except to satisfy the City's payment obligations with respect to outstanding Unlimited Tax Bonds;
- ii. On Count Two, declaring that (i) the City is a conduit for the Restricted Funds and lacks any equitable or beneficial property interest in the Restricted Funds, and (ii) Bondholders and Plaintiffs, as the Bondholders' subrogees, have equitable and beneficial property interests in the Restricted Funds;
- iii. On Count Three, declaring that Bondholders and Plaintiffs, as the Bondholders' subrogees, have a statutory lien on the Restricted Funds within the meaning of 11 U.S.C. § 101(53);
- iv. On Count Four, declaring that Bondholders and Plaintiffs, as the Bondholders' subrogees, have a lien on the Restricted Funds, which constitutes a lien on special revenues within the meaning of 11 U.S.C. §§ 902(2)(E), 922(d), and 928;

- v. On Count Five, declaring that the City's diversion of the Restricted Funds or grant of any postpetition interest in the Restricted Funds to any creditor or any other person or any other impairment of the Bondholders' and Plaintiffs' property interests in the Restricted Funds, without just compensation, is an unlawful taking under the Fifth and Fourteenth Amendments to the United States Constitution;
- vi. On Count Six, declaring that, under Michigan law, as *ad valorem* taxes are collected under the Unlimited Tax Levy, the Restricted Funds must be segregated and deposited, as allocable to each series of Unlimited Tax Bonds, into the related Debt Retirement Funds, and (ii) not commingled with other funds of the City or used for any purpose other than repaying the Bondholders (or Plaintiffs as the Bondholders' subrogees); and
- vii. On all Counts, such other and further relief to Plaintiffs as the Court may deem proper.<sup>6</sup>

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<sup>6</sup> Plaintiffs seek only declaratory relief in this Amended Complaint to establish their property interests in, and the City's obligations with respect to, the Restricted Funds under Michigan Law and the United States Constitution. Consequently, the disposition of Plaintiffs' claims in this adversary proceeding does not require this Court to determine at this time whether Plaintiffs are entitled to adequate protection, although Plaintiffs reserve the right to seek adequate protection based upon the Court's rulings.

Dated: December 23, 2013

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## EXHIBITS

- Exhibit A** City of Detroit Proposals to Voters
- Exhibit B** Michigan Constitution of 1963, Article IX, Section 6
- Exhibit C** Revised Municipal Finance Act (Act 34 of 2001)
- Exhibit D** The Unlimited Tax Election Act (Act 189 of 1979)
- Exhibit E** The Bond Resolutions
- Exhibit F** The Home Rule City Act (Act 279 of 1909)
- Exhibit G** Local Financial Stability and Choice Act (Act 436 of 2012)
- Exhibit H** City of Detroit Proposal for Creditors (June 14, 2013)
- Exhibit I** Specimens of the National-Insured Bonds
- Exhibit J** The National Policies
- Exhibit K** The Sale Orders
- Exhibit L** Specimens of the Assured-Insured Bonds
- Exhibit M** The Assured Policies
- Exhibit N** The Uniform Budgeting and Accounting Act (Act 2 of 1968)
- Exhibit O** State of Michigan Attorney General Opinion (February 19, 1982)
- Exhibit P** 2008 Official Statement (Excerpts)
- Exhibit Q** City of Detroit, Proposed Capital Agenda for Fiscal Years 2004-05 to 2009-10 (Excerpt)
- Exhibit R** City of Detroit Comprehensive Annual Financial Report for the Fiscal Year Ended June 30, 2012 (Excerpts)

- Exhibit S** City of Detroit, Proposed Capital Agenda for Fiscal Years 2013-14 to 2017-18 (Excerpt)
- Exhibit T** Emergency Manager Order No. 12
- Exhibit U** City of Detroit Ten-Year Plan (Excerpt)
- Exhibit V** The Demand Letter