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Legal News Delivered
A publication of Jaffe Raitt Heuer & Weiss
October, 2016

Sixth Circuit Court of Appeals Upholds Constitutionality of Michigan Emergency Manager Law

Judith Greenstone Miller*, Partner
Paul R. Hage, Partner**
Jaffe Raitt Heuer & Weiss, P.C.

On September 12, 2016, the United States Court of Appeals for the Sixth Circuit, affirmed, in *Phillips v. Snyder*., __ F.3d. __, 2016 WL 4728026 (6th Cir. 2016), the lower court decision of Judge George C. Steeh of the United States District Court for the Eastern District of Michigan, dismissing a complaint challenging the constitutionality of Michigan's Local Financial Stability and Choice Act, PA 436, a statute allowing for the temporary appointment of an emergency manager for a municipality or public school system facing a financial crisis. The complaint was filed by voters and local elected officials from areas in Michigan with emergency managers[1]. Judge Rogers wrote the opinion for the Court, in which Judges Griffin and Suhrheinrich joined.

The Parties and the Constitutional Challenges:

The plaintiffs/appellees were individual voters and local elected officials in areas in which Michigan Governor Richard Snyder had appointed an emergency manager under PA 436, after finding that a financial emergency existed. The plaintiffs filed suit and contended that PA 436 was unconstitutional by "vesting elected officials' powers in appointed individuals [i.e., temporary emergency managers]" and violated their right to elect local legislative officials under the following constitutional provisions and federal statutes:

(i) the Due Process Clause of the Fourteenth Amendment to the United States Constitution;

(ii) the Guarantee Clause of Article IV, § 4 of the United States Constitution, which guarantees a republican form of government;

(iii) the Fourteenth Amendment's Equal Protection Clause, by burdening their right to vote and by discrimi nating against African Americans, the poor, and those entities that had emergency managers under the previous laws;

(iv) § 2 of the Voting Rights Act;

(v) the First Amendment of the Constitution by engaging in viewpoint discriminating and infringing on plaintiffs' freedom of speech, freedom of association, and right to petition their government; and

(vi) the Thirteenth Amendment of the Constitution.

1 The plaintiffs are voters and elected officials from Detroit, Pontiac, Benton Harbor, Flint and Redford, all municipalities in which emergency managers had been appointed under PA 436.

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The District Court Decision:

The District Court found that the plaintiffs had standing to bring the suit because they were residents of the cities with emergency managers. Thus, they were held to have alleged harm unique to residents living in cities where elected officials were displaced. Turning to the merits, the District Court dismissed almost all of the plaintiffs' claims. First, it held that the Fourteenth Amendment does not contain a fundamental right to elect local officials. Second, the Guarantee Clause, the Court held, does not apply to local governments. Third, the Equal Protection Clause, which protects the right to vote on equal footing in a particular jurisdiction, was not violated. Fourth, the Equal Protection claim, based on discrimination, was also dismissed because PA 436 did not restrict the plaintiffs' ability to vote based on their wealth. Moreover, the Court held that PA 436 had a "rational basis" for any differential treatment. Fifth, the Voting Rights Act was not violated because PA 436 did not impose any impediment to voting. Sixth, the First Amendment claims failed because PA 436 did not infringe on any speech rights. Seventh, the Court dismissed the challenge under the Thirteenth Amendment finding that the plaintiffs still had available to them what the Court deemed "every device in the political arsenal." The Court also refused to dismiss the Equal Protection claim based on discrimination against African Americans. However, because the parties thereafter stipulated to a dismissal of this claim, it was not part of the pending appeal.

The Opinion of the Court of Appeals:

Holding:

The Court of Appeals concluded that '[b]ecause the relevant constitutional and statutory provisions [did] not support relief for plaintiff, the district court's dismissal of the claims was proper" and should be dismissed under Fed.R.Civ.P. 12(b)(6).[2]

Analysis of the Court of Appeals:

On appeal, the Sixth Circuit Court of Appeals first confirmed that the plaintiffs[3] had standing because they had suffered "concrete and particularized" injuries. Their "alleged

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2 Fed.R.Civ.P. 12(b)(6) allows a court to dismiss a complaint if it determines that the complaint "fails to state a claim upon which relief may be granted."

3 Although one of the plaintiffs, Glass, a resident from Redford, Michigan, was not found to have standing because Redford had not been subject to the appointment of an emergency manager, nevertheless, the Court held that, to the extent the

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deprivations stem[ed] directly from application of PA 436 to plaintiffs' cities or schools," the Court found, and plaintiffs' alleged injuries would be redressed by a decision favorable to them.[4]

Turning to the merits, the Court began its analysis by examining the statutory scheme developed in Michigan for dealing with municipal insolvency, beginning with PA 101 in 1988,[5] which allowed the state to appoint emergency financial managers over cities experiencing a financial emergency, followed by PA 72 (which replaced PA 101 in 1990), which provided for an emergency review board to appoint an emergency financial manager for a local government only after the governor had declared that a financial emergency existed or, alternatively, for consent agreements entered into by the respective municipality. In 2011, PA 72 was repealed and replaced with PA 4,[6] which changed the name from an "emergency financial manager" to an "emergency manager" and further expanded the scope of the powers granted to an emergency manager over the conduct of the local government. PA 4 also made clear that the emergency manager acted "for and on behalf of" the municipality's elected governing board. *See* PA 4 § 19(2). Thereafter, PA 4 was suspended after petitions to place a referendum on the ballot in 2012 to reject the act were successfully initiated. PA 4 was then rejected by the voters in November 2012. Thereafter, Michigan passed PA 436, which again allowed for (i) the appointment of an emergency manager for eighteen (18) months with broad powers over the local government, (ii) four (4) options for a local government confronted with a finding of a financial emergency,[7] and (iii) removal an emergency manager before completing his term.[8] It is this law which underlies the current framework for dealing with municipal insolvencies in Michigan and the act which is challenged in this lawsuit. The Court analyzed and dismissed each of the claims raised by the plaintiffs.

With respect to the plaintiffs' first claim, that they were deprived of substantive due process – the right to vote for individual(s) exercising legislative power at the local level – through the appointment of an emergency manager under PA 436, the Court held that this argument lacked merit and was inconsistent with the Supreme Court's holdings that "states have 'absolute discretion' in allocating powers to their political subdivisions (and therefore to the officers running those subdivisions), which are 'convenient agencies' created by the states." The plaintiffs had primarily relied on an earlier Supreme Court decision in *Reynolds v. Simms*, 377

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4 The Court also refused to dismiss alleged moot claims for equitable relief by plaintiffs from Benton Harbor and the Detroit Public Schools as their claims were indistinguishable from the claims of the other non-moot plaintiffs.

5 Local Government Fiscal Responsibility Act.

6 Local Government and School District Fiscal Accountability Act.

7 MCL § 141.1547(1)(a)-(d).

8 MCL § 141.1549(11). PA 436 provides, among other things, for (i) the automatic conversion of emergency financial

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U.S. 533 (1964), which provided that "each and every citizen has an inalienable right to full and effective participation in the political processes of [a] State's legislative bodies," to support this argument. The Court dismissed this argument as "meritless" and held that states may allocate powers of subsidiary bodies among elected and non-elected leaders and policy makers and there is no fundamental right to have local officials elected or selected by popular vote. Thus, according to the Court, "a state has the power to decide not to select local officials by election." While the *Reynolds* case protects a right to vote for state legislators on equal footing with other votes in the state, having "equal access" does not imply that certain officials must be elected. Finally, the Court reiterated that due process is only implicated "in the exceptional case where a state's voting system is fundamentally unfair," and "not when a state decides to appoint local officials instead of having them elected."

The next argument raised by the plaintiffs and disposed of by the Court was that PA 436 deprived them of the Constitution's guarantee of a republican form of government in Article IV. In essence, PA 436, and the appointment of an emergency manager thereunder, according to the plaintiffs, deprived them of the form of government of a political subdivision they were entitled to in violation of this Constitutional guarantee. Consistent with its tradition, the Court held that "claims brought under the Guarantee Clause are nonjusticiable political questions." "[I]t is up to the political branches of the federal government to determine whether a state has met its federal constitutional obligation to maintain a republican form of government." Ultimately, how power is distributed by a state is a question for the state itself.

The plaintiffs next argued that PA 436 violated the Equal Protection Clause by, among other things, (i) treating emergency financial managers under PA 72 differently than emergency managers appointed under PA 436, and (ii) impairing their right to vote for local elected officials. The Court again dismissed these arguments as there was a "rational relationship to a legitimate governmental purpose" associated with PA 436 – *i.e.,* providing for conditions to deal with and improve a financially distressed municipality. Nevertheless, the plaintiffs argued that financial emergency managers appointed under PA 72 were treated differently than emergency managers appointed under PA 436 by virtue of the fact that upon enactment of PA 436, the emergency financial managers appointed under PA 72 were automatically converted to emergency managers under PA 436, and thus, they served in those positions longer than the 18-month period provided for emergency managers appointed under PA 436.[9] The Court held that just because an individual may serve in their position a longer period of time by virtue of this change did not mean that PA 436 treats them in a discriminatory manner, particularly since at the time of enactment of PA 436, individuals initially appointed under PA 72 were under the same strictures as individuals appointed under PA 436. As for the alleged deprivation of the right to vote, the Court reiterated that the right to vote was not impacted because (i) the local elected officials were not removed but rather the powers of the local government were temporarily vested in an emergency manager, and (ii) the plaintiffs had failed to demonstrate that "they [had] been denied the right to vote on equal footing within their respective jurisdictions." Finally, the plaintiffs unsuccessfully attempted to argue that PA 436 was not rational because it

9 MCL 141.1548(6)(c) provides that an emergency financial manager appointed under PA 72 that is still serving at the time of the enactment of PA 436 is deemed to be an emergency manager under PA 436.

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discriminated on the basis of race and wealth and, thus, the Court should strictly scrutinize the act. The Court held that stricter scrutiny was not merited for alleged "district wealth discrimination," which the Court found was not the type of class saddled with disabilities and the traditional indicia of purposeful, unequal treatment. Further, the Court found that solvency of a municipality does not necessarily correlate with the wealth of an individual locality's residents – rather, they are two separate concepts, not impacting the Equal Protection Clause.

The Court then dismissed the plaintiffs' argument that the appointment of an emergency manager under PA 436 violated § 2 of the Voting Rights Act[10] by depriving them of their right to vote. The Court held, consistent with prior decisions, that this section of the Voting Rights Act does not cover appointive systems or a state's choice between having an elective versus an appointive system. The Michigan legislature was thus within its rights to allocate the powers under PA 436 to an emergency manager appointed by the governor, as opposed to an elected individual. The appointment itself did not replace an elected official or otherwise involve "a voting qualification or prerequisite to voting standard, practice or procedure resulting in the denial of a right to vote."

The plaintiffs next argued that because the voters in Michigan had previously vetoed by referendum PA 4, their ability to express their views – *i.e.*, First Amendment rights to freedom of speech and to freedom of association – had been infringed. This argument was also dismissed by the Court. First, the plaintiffs had admitted that PA 436 was different than PA 4. Second, the fact that a legislature passes laws similar to previously vetoed laws, according to the Court, "does not restrict the expression of one's viewpoint." Moreover, the Court pointed to the provisions of PA 436 that allow for removal of an emergency manager,[11] thereby providing the citizens with the right to advocate for such action, and thus, PA 436 does not abridge plaintiffs' First Amendment rights.

The final argument raised by the plaintiffs rested on the Thirteenth Amendment. The plaintiffs argued that PA 436 acted as a "badge or incident of slavery." Finding that there was no direct connection to race in PA 436 and that the statute was entirely facially neutral with respect to race, the Court could not find any "odious practice the Thirteenth Amendment was designed to eradicate" and the plaintiffs had not cited any case law to support such an alleged violation. Moreover, the Court noted that PA 436 – the state's remedy for financially distressed communities – was passed by "state-elected bodies for which African-Americans have a constitutionally protected right to vote.

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10 Section 2 of the Voting Rights Act provides that "[n]o voting qualification or prerequisite to voting or standard, practice, or procedure shall be imposed or applied . . . which results in a denial or abridgement of the right of any citizen . . . to vote on account of race or color." 52 U.S.C. § 10301(a).

11 MCL §§ 141.1549(11) (removal process before expiration of 18 months) and 141.1549(6)(c) (removal process after expiration of 18 months).

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Petition for Rehearing *En Banc* Sought:

No appeal has yet been taken from this ruling. However, plaintiffs sought and, the Court granted, a 14-day extension to request a rehearing *en banc*. The plaintiffs filed their petition for rehearing on October 11, 2016. The plaintiffs argue, among other things, that "[n]o state in the history of the nation has adopted a law like . . . PA 436 [and] [n]o court in this nation has constitutionally scrutinized such a law." Moreover, they contend that "the panel's decision radically conflict[ed] with decisions of both the United States Supreme Court and this Honorable Court" and the "case involves questions of precedent-setting error of exceptional importance that have not been before any court," to wit: the transfer of governing power, including general legislative powers, to an appointed emergency manager, thereby impairing the voting rights of all citizens in the community and disproportionately used in African-American communities. In this regard, the plaintiffs allege that 52% of Michigan's African-American population was subject to governance by an emergency manager at the time that they filed their complaint in March 2013.

The plaintiffs noted several errors by the panel that they contend "radically departed from existing standards" to justify a hearing *en banc* and reconsideration, including:

- The panel proceeded directly to review the ultimate merits of the plaintiffs' claims without first permitting factual development and ignoring the well-pled facts of the plaintiffs and injecting their own facts; thus, dismiss al under Federal Rule of Civil Procedure 12(b)(6) was not appropriate unless there was a finding that there was no set of facts that would allow the plaintiffs to recover;

- The panel supplanted established standards of review for the Fourteenth Amendment substantive due process, Guarantee Clause and the Thirteenth Amendment claims, inconsistent with decisions of the Supreme Court and the Sixth Circuit Court of Appeals, thereby effectively finding that voting rights in their entirety are not protect ed by these constitutional provisions;

- The panel rejected case law standards from other Supreme Court decisions to find that (i) there was no funda mental right to vote, and (ii) a state has absolute discretion to manipulate its subdivisions and diminish voting rights within classes of voters created by the actions of the state itself;

- The panel erroneously found that *Harper v. Va. State Board of Elections*, 383 U.S. 663 (1966) was overruled, thereby resulting in the panel becoming the first federal court in the nation to now find that wealth based voting criteria are permitted under the Equal Protection Clause; and

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- The panel misapplied the law interpreting the totality of circumstances standard of § 2 of the Voting Rights Act.

If the Sixth Circuit Court of Appeals grants the petition, a subsequent hearing will be held by the entire bench of the Sixth Circuit. If, however, the petition is denied, the plaintiffs' sole recourse will be to file a petition for writ of certiorari with the United States Supreme Court. Because of the limited number of cases accepted for review by the Supreme Court, and the standards governing the grant of certiorari, if the plaintiffs lose at the Sixth Circuit and are forced to pursue review by the highest court, they will face a difficult road.

* Judith Greenstone Miller is a partner in the Southfield office where she is a member of the Firm's Insolvency and Reorganization and Privacy and Datasecurity Practice Group. She specializes in credi tors' rights and commercial litigation. Her practice involves representing debtors, secured and unsecured creditors, creditors' committees and trustees in bankruptcy proceedings, primarily involving Chapter 11 reorganizations and municipal restructuring.

** Paul Hage is a partner in the Southfield office where he is a member of the Firm's Insolvency and Reorganization Practice Group, specializing in representing asset purchasers, unsecured creditors' committees, debtors, secured and unsecured creditors, and trustees in bankruptcy proceedings and municipal restructuring.

Jaffe Raitt Heuer & Weiss is a firm of over 100 lawyers with a broad, business-oriented practice. The firm is organized into several specialized practice groups. Jaffe's Insolvency and Reorganization Practice Group concentrates exclusively in areas related to insolvent and financially troubled entities, including bankruptcies, reorganizations, liquidations, municipal restructurings (both under P.A. 436 and under Chapter 9), loan and lease restructuring and enforcement, forbearance and composition arrangements, out-of-court workouts, preference and fraudulent conveyance prosecution and defense, surrender arrangements, bulk sales transfers, foreclosures, collections, receivership proceedings and related litigation and appellate matters.

For additional information contact Judith Greenstone Miller at jmiller@jaffelaw.com or Paul Hage at phage@jaffelaw.com or at 248.351.3000

Jaffe
JAFFE RAITT HEUER & WEISS
A Professional Corporation
Attorneys & Counselors

27777 FRANKLIN ROAD • SUITE 2500 • SOUTHFIELD, MICHIGAN 48034
PHONE: 248.351.3000 • FAX: 248.351.3082
SOUTHFIELD • DETROIT
ANN ARBOR • NAPLES
www.jaffelaw.com