UNITED STATES BANKRUPTCY COURT EASTERN DISTRICT OF MICHIGAN SOUTHERN DIVISION

IN RE: CITY OF DETROIT, Docket No. 13-53846
MICHIGAN, Detroit, Michigan September 29, 2014

Debtor. 8:30 a.m.

LYDA, et al., Adv. No. 14-04732

Plaintiffs, Defendant.

HEARING RE. RE. (#20) MOTION FOR TEMPORARY RESTRAINING ORDER FILED BY PLAINTIFFS SCOTT EUBANK, NICOLE HILL, JOANN JACKSON, MAURIKIA LYDA, MICHIGAN WELFARE RIGHTS ORGANIZATION, MORATORIUM NOW!, NATIONAL ACTION NETWORK-MICHIGAN CHAPTER, ANNETTE PARHAM, PEOPLES WATER BOARD, JOHN SMITH, SYLVIA TAYLOR, ROSALYN WALKER, JANICE WARD, TAMMIKA WILLIAMS (ATTACHMENTS: #1 EXHIBIT 2 NOTICE AND OPPORTUNITY FOR HEARING #2 EXHIBIT 3 BRIEF IN SUPPORT OF MOTION FOR TRO #3 EXHIBIT 4 CERTIFICATE OF SERVICE #4 EXHIBIT 5 PART ONE #5 EXHIBIT 5 PART 2 #6 EXHIBIT 5 PART TWO (EXTRA PAGE) #7 EXHIBIT 5 PART 3 #8 EXHIBIT 5 PARTS FOUR AND FIVE #9 EXHIBIT 5 PART SIX #10 EXHIBIT 5 PART 7 #11 EXHIBIT 6 INDEX #12 EXHIBIT 6 PART 1 #13 EXHIBIT 6 PART 2 #14 EXHIBIT 6 PART 3 SECTION 1 #15 EXHIBIT 6 PART 3 SECTION 1 ADDITIONAL PAGE #16 EXHIBIT 6 PART 3 SECTION 2 #17 EXHIBIT 6 PART 4 #18 EXHIBIT 6 PART 5 #19 EXHIBIT 6 PART 6); (#26) MOTION TO DISMISS ADVERSARY PROCEEDING RE. INABILITY TO GRANT RELIEF AND FAILURE TO STATE A CLAIM FILED BY DEFENDANT CITY OF DETROIT, MICHIGAN BEFORE THE HONORABLE STEVEN W. RHODES UNITED STATES BANKRUPTCY COURT JUDGE

APPEARANCES:

For Plaintiffs
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Rosalyn Walker,
Annette Parham,
Janice Ward, Sylvia
Taylor, Scott Eubank,
Joann Jackson, Tammika
Williams, Michigan
Welfare Rights
Organization, Peoples
Water Board, National
Action Network-Michigan
Chapter and Moratorium
Now!:

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Proceedings recorded by electronic sound recording, transcript produced by transcription service.

THE CLERK: All rise. Court is in session. You may be seated. Calling Case 14-4732, Lyda, et al., versus City of Detroit, Michigan.

THE COURT: Good morning. Counsel, please place your appearances on the record.

MS. JENNINGS: Alice Jennings on behalf of the plaintiffs, your Honor.

MR. SWANSON: Good morning, your Honor. Marc Swanson from Miller Canfield along with my colleague Soni Mithani and Tom O'Brien.

MS. KAMINSKI: Good morning, your Honor. Shanna
Kaminski on behalf of the City of Detroit Water and Sewerage
Department.

MR. WOLFSON: Good morning, your Honor. William Wolfson, chief administrative officer, chief compliance officer, and general counsel, DWSD.

MR. THORNBLADH: Your Honor, two more appearances for the plaintiff. Kurt Thornbladh on behalf -- can you hear me -- on behalf of the plaintiffs, and also Marilyn Mullane is beside me on behalf of the plaintiffs.

THE COURT: Before the Court are two motions, the plaintiffs' motion for a temporary restraining order or a preliminary injunction and the city's motion to dismiss. The Court will begin with a brief statement of its conclusions on these motions and then review in detail the reasons for its

conclusion.

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The Court finds that the motion to dismiss the complaint must be granted because, one, Section 904 of the Bankruptcy Code prohibits the Court from granting the injunctive relief that the plaintiffs request. Two, while issues arising under Section 365 of the Bankruptcy Code relating to executory contracts do fall within the Court's core jurisdiction, the relationship between the city and its customers is not an executory contract. Even if the relationship were construed to be an executory contract, the relief sought by the plaintiffs in this case is outside the scope of that section and prohibited by Section 904. Three, the plaintiffs' due process and equal protection claims are not subject to Section 904 but, nonetheless, must be dismissed because they fail to state claims upon which relief can be granted. Finally, even if this Court had the authority to grant the relief requested, the Court would not issue a preliminary injunction based on the evidence.

The problems and challenges that the City of Detroit and its residents face run wide and deep. The adversary proceeding that these plaintiffs filed focuses on the alleged failure of the city and its water department to properly address the inability of a large number -- a large portion of the city's residents to pay for water. The complaint contains a number of interesting and creative legal theories

in support of the relief sought. These theories include violations of due process and equal protection, breach of executory contract, public health emergency, estoppel, human right to water, and public trust. The complaint seeks an injunction imposing a six-month moratorium on residential water shutoffs, an injunction requiring that water service be restored to all residents whose water service has been terminated, an order directing the city to implement a water affordability plan with income-based payments for residential customers. It also seeks declaratory relief finding that the city's and the water department's policies, procedures, and actions relating to notice of bills, dispute of bills, opportunities for payment and hearings prior to water service shutoffs violate the due process and equal protection clauses of the Fourteenth Amendment to the United States Constitution. It also seeks declaratory and equitable relief finding that the city's policies, procedures, and actions related to the denial, interference, or deprivation of the plaintiffs' right to use water are protected by the public trust doctrine, the human right to water, and the laws and Constitutions of Michigan and the United States.

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Presently before the Court are the plaintiffs'
motion for a temporary restraining order or preliminary
injunction and the city's motion to dismiss. The city's
motion to dismiss relies on this Court's previous ruling that

Section 904 of the Bankruptcy Code prohibited the Court from allowing the plaintiffs to intervene in the bankruptcy case to pursue its water-related claims. In the Court's order regarding intervention dated August 14, 2014, at Docket 6708, the Court stated, quote, "Unlike other chapters of the bankruptcy code, chapter 9 strictly limits the Court's power in a municipal bankruptcy case. This is to ensure that the separation of powers contemplated in the United States Constitution is upheld and that the Court does not overstep its bounds into the sovereign powers of the states. section 904 of the bankruptcy code prohibits the Court from interfering with, internal quote, '(1) any of the political or governmental powers of the debtor; (2) any of the property or revenues of the debtor; or (3) the debtor's use or enjoyment of any income-producing property, ' close internal quote, 11 U.S.C., Section 904. This limitation means the Court cannot interfere with the 'choices a municipality makes as to what service and benefits it will provide.' In re. Addison Community Hospital Authority, 175 B.R. 646, 649, Bankruptcy, Eastern District of Michigan, 1994, citing H.R. Report Number 595, 398." Continuing with the quote, "Further, this provision makes it clear that 'chapter 9 was created to give courts only enough jurisdiction to provide meaningful assistance to municipalities that require it, not to address the policy matters that such municipalities

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control.' Id. Consequently, given the constraints of Section 904, the Court does not have the authority to require the DWSD to stop mass water shut-offs, to require that DWSD refrain from implementing a program of mass water shut-offs in the future, or require that the DWSD implement procedures regarding rate setting or water affordability plans," close quote.

The city asserts that the order denying intervention was correct under the Bankruptcy Code, Section 904, and that there is no basis now to reach a different result on any of the plaintiffs' claims or requests for relief in the adversary proceeding.

The plaintiffs argue three points in an attempt to save their complaint from the broad reach of Section 904. First, they argue that the city's agreement to provide water services to a resident or customer and that customer's agreement to pay for those services constitutes an executory contract. They argue that Section 904 does not deprive the Court of its authority over the city's assumption or rejection or executory contracts under Section 365 of the Bankruptcy Code because Section 901 of the Bankruptcy Code incorporates Section 365 into Chapter 9.

The plaintiffs are surely correct that despite Section 901 and 904, the Court retains the complete authority that Section 365 gives it. Indeed, the city does not argue

The parties disagree, however, on whether the arrangement between the city and its water customers constitutes an executory contract. This is a complex question under bankruptcy law as the Court's colloquy with counsel for the city on this point demonstrated. On this question, the Court concludes that the arrangement is not an executory contract, although not for the reasons that the city argues. The city argues that its arrangement is simply a series of contracts of one-month terms and that after a one-month term is complete, the city has no executory obligations to perform. Rather, the Court concludes that the arrangement is simply a part of the range of municipal services that the city has determined to provide pursuant to state law and local ordinance. It has assumed that obligation to its residents pursuant to its governmental powers under law. Specifically, MCL 117.4(b) authorizes city charters to provide for the installation of waterworks to provide water services to residents, and the Detroit City Charter so provides in Section 7-1202. MCL 123.166 authorizes a municipality to discontinue water service. states, quote, "A municipality may discontinue water service or sewage system service from the premises against which a lien created by this act has accrued if a person fails to pay the rates, assessments, charges, or rentals for the respective service, or may institute an action for the

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collection of same in any court of competent jurisdiction," close quote. MCL 141.121 requires that water rates be set at the reasonable cost of delivering the service and appears at least by implication to exclude any consideration of ability to pay. Nothing in the Bankruptcy Code, including Section 365, permits the city to, quote, "reject," close quote, or withdraw from that obligation. It is not a mere private party that has contracted to provide water services to customers. The city does so under law.

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The question then becomes whether this legal obligation that the city has assumed to provide water services to residents somehow transforms into an executory contract because the resident is obligated to pay for the service and because the city has the authority to terminate the water services to residents who do not pay for it. Court concludes that the answer to this question remains that the arrangement is not an executory contract. Rather, the arrangement is strictly a matter of law. The law obligates the city to provide the service. The law requires the resident to pay for it. The law allows the city to terminate The Bankruptcy Code, therefore has service for nonpayment. nothing to say in the matter. Section 365 does not authorize the city to assume or reject law. Accordingly, the plaintiffs' argument that its Section 365 claim provides them with an escape from Section 904 must be rejected, and their

executory contract claim must be dismissed.

The second way in which the plaintiffs seek to avoid the sweep of Section 904 and this Court's prior ruling applying it to their claims is to invoke the exception in Section 904 that applies when the city consents to Bankruptcy Court jurisdiction. Specifically, the plaintiffs argue that language in the city's plan of adjustment constitutes the necessary consent. The Court must reject this argument. It finds nothing in the plan of adjustment that the city filed that establishes its consent to Bankruptcy Court jurisdiction over this adversary proceeding.

The third way that the plaintiffs seek to avoid the sweep of Section 904 and this Court's prior ruling applying it to their claims is to invoke this Court's noncore jurisdiction. On this point, it is correct that under 28 U.S.C., Section 1334(b), the Bankruptcy Court has jurisdiction to resolve any issue that is, quote, "related to," close quote, the bankruptcy case. Nevertheless, the Court must reject the plaintiffs' argument if only because it proves way too much. If the plaintiffs are right about Section 1334(b), it would nullify Section 904. Indeed, that Section 904 provides the answer. It states in its opening six words, quote, "Notwithstanding any power of the court," close quote. Surely that includes notwithstanding the Bankruptcy Court's noncore or related to jurisdiction under

Section 1334(b) of Title 28. As stated in Association of Retired Employees of the City of Stockton versus City of Stockton, California, In re. City of Stockton, California, 478 B.R. 8, 20, Bankruptcy, Eastern District of California, 2012, Section 904 is, quote, "so comprehensive that it can only mean that a federal court can use no tool in its toolkit," close quote.

There are, however, two claims made here by the plaintiffs that are not so readily swept away by Section 904. These are the plaintiffs' constitutional claims. As noted, the plaintiffs seek a declaratory judgment that the city billing and service termination procedures violate due process and equal protection. The gravamen of the due process claim is that DWSD fails to follow certain procedures posted on its website and fails to adequately inform customers about the possibility of a hearing on disputed water bills and available aid for paying their water bills. The gravamen of the equal protection claim relates to differing treatment between residential and commercial customers.

The Court concludes that Section 904 of the Bankruptcy Code cannot protect the city from the Bankruptcy Court's jurisdiction over the plaintiffs' constitutional claims because the city does not have the, quote, "governmental power," close quote, to violate the due process

and equal protection mandates of the United States

Constitution. The city must comply with them. Accordingly,

the Court concludes that those claims, unlike the plaintiffs'

other claims, do survive the city's Section 904 challenge.

The city asserts that, nevertheless, these claims are subject to dismissal for failing to state a claim upon which relief can be granted under Rule 12(b)(6) of the Federal Rules of Civil Procedure. Under Bell Atlantic Corp. v. Twombly, 550 U.S. 544, 550, 2007, and Ashcroft v. Iqbal, 556 U.S. 662, 2009, if the complaint does not set forth a plausible claim for relief, it must be dismissed.

In <u>Herrada</u> v. <u>City of Detroit</u>, 275 F.3d 553, 556, Sixth Circuit, 2001, the Sixth Circuit stated, quote, "The Fourteenth amendment to the United States Constitution prohibits states from depriving citizens of 'life, liberty, or property' without 'due process of law.' A two-step analysis guides our evaluation of the procedural due process claims. We must first determine 'whether there exists a liberty interest or property interest which has been interfered with by the defendants.' Second, if such a deprivation occurred, we must decide whether the procedures that accompanied the interference were constitutionally sufficient," close quote, citations omitted.

The Court concludes that the plaintiffs' due process claim fails for one simple reason. The plaintiffs cannot

plausibly allege that they have a liberty or property interest in receiving water service let alone water service at a rate based on ability to pay. As the Court found earlier, the city provides water services to its residents under applicable state law and local ordinance, but nothing in those laws establishes the kind of property or liberty interest to which due process rights apply.

Similarly, the Court concludes that the plaintiffs' equal protection claim fails. In Romer v. Evans, 517 U.S. 620, 631, 1996, the United States Supreme Court stated, quote, "The Fourteenth Amendment's promise that no person shall be denied equal protection of the laws must co-exist with the practical necessity that most legislation classifies for one purpose or another, with resulting disadvantage to various groups or persons. We have attempted to reconcile the principle with the reality by stating that, if a law neither burdens a fundamental right nor targets a suspect class, we will uphold the legislative classification so long as it bears a rational relation to some legitimate end," close quote.

Here the plaintiffs simply allege that there are delinquent commercial account customers whose water service has not been disconnected or where there has been a disconnection DWSD, quote, "failed to terminate services for those enterprises in the manner used for residential

customers," close quote. But under Romer v. Evans, this is not enough. The plaintiffs do not allege that they have a fundamental right to water service. Indeed, they have cited no state or federal law, whether statutory law or common law, that so provides here in Michigan. Further, the plaintiffs do not allege that residential customers are a suspect class for equal protection purposes. They simply argue that there is no rational basis for the alleged difference in treatment between residential and commercial customers. In Twombly cited earlier, the Supreme Court stated that while a court must accept all factual content in pleading -- in the pleading as true, it is not bound to accept as true a legal conclusion couched as a factual allegation, 550 U.S. at 555. In <u>Igbal</u>, also cited earlier, the Supreme Court stated that a court considering a motion to dismiss can choose to begin by identifying pleadings that, because they are no more than conclusions, are not entitled to the assumption of truth, 556 U.S. at 678.

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The Court concludes that the fact that some commercial customers have not been disconnected while some residential customers have been disconnected does not establish a violation of equal protection. Moreover, the Court finds that there is a rational basis for the differing treatment. Some commercial customers have more complex service connections and, therefore, more complex

disconnection procedures. Accordingly, the Court concludes that the complaint must be dismissed.

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Technically, this renders the plaintiffs' motion for preliminary injunction moot, but the Court concludes that it should be addressed in the alternative here. In deciding whether to issue a preliminary injunction, the Court balances the following four factors: whether the movant has a strong likelihood of success on the merits; whether the movant would otherwise suffer irreparable injury; whether the issuance of a preliminary injunction would cause substantial harm to others, including the party opposing the motion; and whether the public interest would be served by the issuance of a preliminary injunction. McPherson versus Michigan High School Athletic Association, 119 F.3d 453, 459, Sixth Circuit, 1997, en banc. These four factors should be balanced against one another and are not to be treated as threshold requirements for the grant of a preliminary injunction, Leary versus Daeschner, 228 F.3d 729, 736, Sixth Circuit, 2000.

Based on the evidence before it, the Court makes the following findings. Exhibit 12 and Exhibits 107(a) through (h) are customer bills. The reverse side of the bill has a paragraph at the bottom captioned "Complaints and Disputes." It states, quote, "It is the customer's responsibility to inform the utility of any billing dispute. A monthly billed

customer may dispute a bill no later than 28 days after the billing date. After the period to dispute expires, the customer forfeits the right to dispute the bill. All amounts not in dispute are due and payable. For additional information, you may visit us on line at www.dwsd.org," close quote. Exhibit 120, the interim collection rules and procedures, sets forth the detailed complaint and shutoff procedures and is available on the website.

In this case, there is no evidence that the customers dispute their water bills with any significant frequency. Rather, disputes appear to be rare. None of the water customers who testified stated a dispute regarding their water bill or an inability to access the city's dispute process. In one respect, the city, however, no longer follows the procedures that it publishes on its website. It no longer makes personal visits to customers who are in shutoff status. It is now considered unnecessary and imprudent for DWSD employees. Accordingly, the city is preparing revised rules and procedures.

In another respect, the city's adherence to its policies is uneven. Specifically by policy, for certain customers with special needs such as medical conditions or with children, service terminations may be delayed or adjusted. It does appear, however, that most -- excuse me -- that most customers are unaware of this or do not know how to

pursue this relief, and, as a result, some service terminations occur that should have been delayed.

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Customers fail to pay their water bills for one of three reasons. One, they have the resources to pay but choose not to pay. Two, they have a temporary interruption in their income that deprives them of the resources to pay. Three, their income is fixed and so low that they are chronically unable to pay all of their bills when due, including their water bills. Of course, the city does not know which customers fall into which groups. It only knows and knew that it had an unreasonably and unacceptably high rate of default and delinquency totaling approximately \$87 To address this problem created by these defaults million. and delinquencies, the city quite properly and justifiably embarked upon its program to terminate service in order to motivate payment by those who could. Specifically, the policy became that service would be shut off to any customer in default over \$150 for more than two months. In this program, the city terminated water service to approximately 24,000 customers in 2013 and 19,500 customers this year. this process, however, the city initially neglected to address the needs of its customers in the second and third That motivated the motion to intervene that the Court mentioned earlier and this Court's subsequent suggestion to the city that it find ways of enhancing its

outreach to those customers. The city then developed and executed its ten-point plan in August. In the Court's judgment, this was a bold, commendable, and necessarily aggressive plan. It appears that it has also been generally successful in providing necessary assistance to customers in the group who had temporary income reductions by affording them time as well as help from charities in curing their defaults. This program has led to a significant number of service restorations. There remain, however, thousands of customers whose service was terminated and not restored. is less clear, therefore, that the city's ten-point plan will be of any long-term assistance to the customers in the third group, those with insufficient income to pay their bills. Because the poverty rate in the city is approximately 40 to 55 percent, this may well be a large group. The ten-point plan relies on a combination of charity and public funds to address this need, but there has been no analysis of whether the resources available will be sufficient to meet the needs of the customers in this group over the long term. As the Court held earlier, addressing this important and urgent issue is foreclosed to this Court by Section 904. Still, the Court urges the city to examine this issue with a sense of urgency that it deserves not only because these customers need help but also because it is in the city's best interest. In any event, even if the complaint were not dismissed on

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jurisdictional grounds under Section 904 of the Bankruptcy Court -- Bankruptcy Code, the Court could not find a strong likelihood of success on the merits.

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On the issue of irreparable harm, it appears that none of the plaintiffs are currently without water service, although some did experience periods of service terminations in the past. More generally, however, the Court must conclude that a customer whose water service is discontinued does likely suffer irreparable harm, especially if the service is lost for more than a few days. These harms include the risk of serious and even life-threatening medical conditions as well as adverse consequences in employment, in family and personal relations, and for children in their education. It cannot be doubted that water is a necessary ingredient for sustaining life. It is, however, important to pause here to emphasize that these findings about the irreparable harm that customers may suffer upon termination of their water service does not suggest that there is a fundamental enforceable right to free or affordable water. There is no such right in law just as there is no such affordable right to other necessities of life such as shelter, food, or medical care.

The city argues that the harm is not irreparable because there are alternative sources available, including purchasing containers of water at local stores. The Court

rejects this argument for at least two reasons. First, it is much more expensive, and many of the affected people are already in poverty. Second, it is challenging to commit the time and energy necessary to obtain sufficient quantities of water, especially for those with special needs or single parents with young children. The city also points out that health -- official health department records fail to demonstrate any health consequences from the water shutoffs That appears to be true as far as it goes. However, those record compilations do not appear to be designed to measure or address the consequences of significant water terminations in the city, and there may be a time lag in their compilation. Accordingly, the Court is not prepared to accept the city's suggestion that these records establish that there have not been and will not be any significant health consequences resulting from the water terminations.

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Turning now to the harm that the city might experience if the requested relief is granted, the Court must conclude that it would be significant. The Court finds substantial merit in the city's concern that a six-month injunction against terminations would increase its customer default rate and seriously threaten its revenues, and the Court so concludes even though the city normally would not execute service terminations during a good part of that time

due to freezing weather conditions. The evidence, especially Exhibit 125, establishes an impressively close correlation between shutoffs and collections, and here the Court would pause parenthetically to note that Exhibit 125 was admitted at the hearing. It was, however, mistakenly referred to during the hearing as Exhibit 25, which created some confusion. The Court would further note that Exhibit 126 about which there was a question was not offered or admitted into evidence.

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The context of the city's concern here is extremely important. Detroit cannot afford any revenue slippage, and its obligations to its creditors requires it to take all reasonable and businesslike measures to collect the debts that are owed to it. As it prepares to show the Court that its plan is feasible and as it undertakes its preparations with its hope that the Court will confirm the plan, like any debtor would do in similar circumstances, the last thing it needs is this hit to its revenues that would inevitably result from the injunction that the plaintiffs request. More specifically, the evidence establishes that the city is justifiably concerned about the impact that the requested injunction might have in the continuing development of the Great Lakes Water Authority. This Court has found on the record that this is an important initiative. Any threat to it must be seriously considered. If successfully

implemented, this initiative could achieve the basic democratic goal of giving all of the customers of the DWSD an opportunity to participate in its governance. Equally significantly, it also carries the potential to continue and enhance the political momentum for the kind of broader regional cooperation that many urban areas have found to be absolutely critical in their economic revitalizations. It was precisely for these reasons that the Court granted Wayne County's motion to refer this matter to mediation.

On the issue of public interest, the Court concludes that it largely overlaps with the interests of the city and the region, which the Court has already addressed.

In sum, the Court is faced with an injunction request that is weakly supported by any substantial likelihood of success on the merits, strongly supported by significant evidence of irreparable harm, and strongly undermined by significant evidence of harm to the opposing party here, the city, and the public. On balance and in the Court's discretion, the Court would not issue the requested injunction in these circumstances assuming that it did have the authority to do so. In the Court's view, it is simply inappropriate to invoke such a significant remedy as an injunction when the likelihood of ultimate success is so remote even if the harm to the plaintiffs is otherwise irreparable and especially when the harm to the defendant may

be so substantial.

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One final consideration also suggests that the requested injunction should be denied. As noted, the plaintiffs seek a six-month prohibition on water terminations and a restoration of service for all of the customers whose service was discontinued. Certainly this will provide shortterm relief to those customers who would otherwise be terminated or whose service would be restored by these -- by the requested injunction; however, by itself this relief solves no long-term problems for the customers who chronically cannot pay their bills. It must, therefore, only be a means to an end, but what is that end? The plaintiffs have not provided the Court with a clear picture of what that end looks like in six months nor with a clear roadmap of how to get there. In these circumstances, the Court must conclude that it would be imprudent to grant the injunctive relief that the plaintiffs seek. The Court will prepare an appropriate order.

(Proceedings concluded at 9:06 a.m.)

INDEX

WITNESSES:

None

EXHIBITS:

None

I certify that the foregoing is a correct transcript from the sound recording of the proceedings in the above-entitled matter.

/s/ Lois Garrett

October 1, 2014

Lois Garrett