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WSJ: Bondholders, Public Pensioners Square Off in Detroit.

The bankruptcy case in Detroit could be titled Bondholders v. Pensioners.

The city's emergency manager has said his goal is to spread the pain around. That means goring two sacred cows: general obligation debt and public employee pension benefits.

Both sides are fighting fiercely to prevent that from happening, with each warning of dire consequences.

Last month bondholders winced at the restructuring plan floated by Detroit Emergency Manager Kevyn Orr, who proposed breaking the city's promises to general obligation bond holders.

Backed by the full faith and credit of the issuer, general-obligation debt is regarded as the gold standard of the municipal bond market. But under Mr. Orr's plan, bondholders would stand to lose about $500 million.

That's just a small part of the $11.5 billion in unsecured debt that Mr. Orr put on the chopping block. But it set off investor alarms.

"We believe breaking the promise to GO bondholders and treating all unsecured creditors equally could set a dangerous precedent with far-reaching implications — in Detroit, in Michigan and beyond," wrote Peter J. Hayes, managing director and head of the Municipal Bonds Group for BlackRock, in an op-ed in Thursday's Detroit Free Press.

"This is Wall Street's worst nightmare," Richard Brodsky, a former Democratic New York assemblyman who is advising the mayor of Yonkers, N.Y., on managing the city's finances, told Law Blog. "They have to sit at the table like an equal with the unions and the taxpayers."

Pushing back just as hard against the restructuring plan are Detroit's unions and the city pension boards, which sued to block Thursday's bankruptcy filing.

Slashing retiree health-care benefit plans is one thing. Cutting pension payments to active and retired employees would be a deeply traumatic development for public-sector unions in Detroit and beyond. Estimating a $3.5 billion shortfall in the city's two retirement funds, Mr. Orr has said the city has no choice but to roll back pension benefits.

Like New York, Michigan is constitutionally prohibited from "diminishing" pension benefits already granted to current and retired workers. But federal law could very well trump state law here. The question is whether a federal judge would approve it.

It's all part of Mr. Orr's goal of shared sacrifice. "He really has made enemies with everyone," Stephen Eide, a public-finance analyst at the Manhattan Institute, a conservative think tank in New York City, told Law Blog. "He's made good on that approach."

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