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NYT: Detroit Plan Is Said to Split Creditors Into 2 Groups.

Detroit is preparing to resolve its bankruptcy case by splitting its unsecured creditors into two groups and treating them differently, according to people briefed on the city's plan.

One group, composed of retired city workers, would get cash for their claims, while others, holders and insurers of certain city debts, would get a series of notes of uncertain but lesser value. One person, who asked not to be identified because of a confidentiality order, called the plan "massively discriminatory."

It is a fundamental principle of United States bankruptcy law that similarly situated creditors are treated equitably. In Detroit's bankruptcy case, both the pensioners and the general obligation bondholders are eager to avoid a court precedent where one group would be privileged above another.

Some creditors view the city's proposal, presented in sometimes tense meetings with a mediator, as a blunt negotiating tool meant to cudgel them into accepting unfavorable terms, one of the people briefed on it said.

The city is expected to file a plan with the bankruptcy court by Feb. 17. After that, creditors will file any objections. Detroit's bankruptcy judge, Steven Rhodes, must eventually decide whether the plan is fair and equitable.

Creditors slated to get smaller recoveries were said to be considering their legal options. The bankruptcy judge, mediators and other officials shepherding Detroit through its bankruptcy case have repeatedly urged the parties to reach out-of-court settlements and avoid litigation. The city has more than 100,000 creditors, and there are fears that the city might become hopelessly bogged down if a string of protracted lawsuits is started.

The people briefed on the plan said it contained a "base scenario" in which cash and notes worth $4.2 billion would be divided among the unsecured creditors. Retirees would get cash worth roughly 50 percent of their claims over time, while holders of debt issued in 2005 to shore up the pension system would get about 10 percent.

The city also described a second possible way in which additional money might be available through a lease of Detroit's water and sewer system. If that deal is completed, the city would propose giving all unsecured creditors an additional 3 percent of their claims, but some would still receive more than others.

Some of the money for the retirees' claims is proposed to come from an arrangement being struck with philanthropic organizations in Michigan, which would give roughly $350 million to the Detroit Institute of Art. Their donations are expected to be matched dollar for dollar by the State of Michigan.

The money would be used to keep valuable artworks in Detroit, but the donors have also agreed to stipulate that it be used to pay the retirees' pensions, to the extent possible.

The proposal included $3.1 billion in cash contributions that Detroit would make to its municipal pension system over the next 40 years, and $500 million to support the city retirees' health plan.

The art proceeds and state appropriations would be divided equally between the city's two pension funds, one for the police and firefighters, and another for all other municipal workers. The cash would be split a little differently, with the police and firefighters' pension fund getting $1.4 billion and the general pension fund getting $1.7 billion.

Recoveries for the financial creditors would come from several types of notes that the city would issue. Some of the notes would give creditors a 20 percent recovery rate, but some of them would also have their claims sharply reduced, leaving them with just 10 percent.

By MARY WILLIAMS WALSH and MICHAEL J. de la MERCED JAN. 30, 2014