Bond Case Briefs

Municipal Finance Law Since 1971

Bloomberg: Detroit Cancels Swaps Forbearance Deal With BofA, UBS.

Detroit won't take legal action for now against Bank of America Corp. and UBS AG (UBSN) over a costly swaps deal, even after canceling a forbearance agreement it reached with the banks in July.

While they continue trying to negotiate an end to the swaps, which cost taxpayers about $4 million a month, the city and the banks will refrain from taking court action against each other, according to Bill Nowling, a spokesman for Detroit's emergency financial manager, Kevyn Orr.

"We basically have a gentleman's agreement," Nowling said in an interview yesterday after the city told U.S. Bankruptcy Judge Steven Rhodes it canceled the forbearance deal on Jan. 31.

The forbearance agreement, reached days before Detroit filed the biggest U.S. municipal bankruptcy, was a kind of truce. Detroit agreed not to sue to cancel the swaps and the banks agreed not to declare the city in default of the contracts, which would have allowed them to try to seize casino tax revenue.

The city and the banks have been trying to reach a settlement that Rhodes will accept. Last month, he rejected a proposal to buy out the swaps for $165 million, saying it was too costly.

Detroit's 4.5 percent sewer bonds that mature in 2035 rose about 3.6 percent today to 84.9 cents on the dollar, according to data compiled by Bloomberg.

$18 Billion

Detroit filed for bankruptcy on July 18 after decades of decline, listing $18 billion in liabilities and saying it couldn't pay creditors while also providing basic city services. Orr has been in court-supervised mediation with creditors including bondholders and pension funds to seek an agreement on cuts.

The swaps were designed to protect against rising interest rates by requiring the banks to pay the city if rates climbed above a certain level. When rates fell, Detroit was required to make monthly payments.

Under a draft debt-adjustment plan sent to creditors last month, Detroit would pay nothing to Bank of America and UBS. While the city said in the plan that it disputes the legitimacy of the swaps, it said it may set aside about $4.2 million a month in a reserve fund in case a court finds them legal. Orr said he may file a debt plan with the court this month.

Last week, the city sued to cancel more than $1.4 billion in pension debt underlying the swaps. That lawsuit didn't seek to cancel the swaps themselves, which have cost taxpayers more than $200 million since 2009.

Casino Revenue

The swaps contracts give the banks the right to seek control of Detroit's casino taxes, which the city pledged as collateral, in the event of a default. In December, Corinne Ball, a lawyer for the city, told Rhodes the casino revenue was one of Detroit's best sources of money.

Ball, a partner at Jones Day, didn't immediately respond to a phone call seeking comment on the termination notice.

Megan Stinson, a spokeswoman for Zurich-based UBS, and Bill Halldin, a spokesman for Charlotte, North Carolina-based Bank of America, declined to comment.

The case is In re City of Detroit, 13-bk-53846, U.S. Bankruptcy Court, Eastern District of Michigan (Detroit).

By Steven Church Feb 7, 2014 9:41 AM PT

To contact the reporter on this story: Steven Church in Wilmington, Delaware at schurch3@bloomberg.net

To contact the editor responsible for this story: Andrew Dunn at adunn8@bloomberg.net