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Muni Market Blasts Detroit Debt Plan.

CHICAGO — A pair of bond insurers that wrap a chunk of Detroit's unsecured debt condemned the debt adjustment plan the city filed in bankruptcy court Friday, saying it would only lead to more litigation.

It was one in a series of negative comments municipal bond market participants directed at the city's proposal to treat general obligation bondholders as unsecured creditors.

The city wants to pay GO holders 20 cents on the dollar. Pensioners would see recovery rates of around 30% on the unfunded portions of their pension plans, and potentially more if an \$820 million arts-for-pensions plan put together by the state and a group of foundations is realized.

"While we understand that favoring pensioners and discriminating against bondholders might be politically popular, we believe this is contrary to bankruptcy law and will result in costly litigation that will hamper the city's emergence from bankruptcy," Steve Spencer, financial advisor to bond insurer Financial Guaranty Insurance Co., the city's largest unsecured creditor, said in a statement.

"Any plan of adjustment that fails to maximize the value of the city's numerous valuable assets to enhance recoveries for creditors will leave billions on the table and fail to meet requirements of bankruptcy law, increasing the chances of drawn-out litigation that nobody wants," he said.

Syncora Guarantee, which, with FGIC, insures the city's \$1.4 billion of pension certificates, also protested the plan, saying Detroit emergency manager Kevyn Orr is leaving "more than half a billion dollars" in potential savings on the table by failing to improve city services or boost revenues.

For the muni market, the city's treatment of unlimited-tax GOs as unsecured has rattled traditional beliefs about the debt being among the safest of investments.

"We have serious concerns about general obligation bonds being treated as unsecured debt," said Leslie Norwood, associate general counsel and co-head of the municipal securities group at the Securities Industry and Financial Markets Association. "We think municipalities, investors, and taxpayers should care about this."

Norwood said that reduced investor confidence in GO bonds could lead to a reduction in market access and higher borrowing costs for Detroit and other Michigan issuers, which will in turn lead to higher taxes on residents.

"It will potentially have impacts not just on Detroit, but on other cities," Norwood said.

Fitch ratings analyst Arlene Bohner said the plan's preferential treatment of pensioners over GO holders is "troubling," an depending on the outcome of the bankruptcy court's decision, could affect Fitch's rating methodology.

"This could potentially cause us to review our policies and change how we view GO bonds in Michigan," Bohner said.

Municipal Market Advisors, in a comment issued Feb. 18, warned that the treatment of unlimited-tax GOs as unsecured could drive up local GO borrowing costs by 25 basis points across the country.

The Bond Dealers of America warning that Detroit's approach to GOs has national implications for the market.

Detroit's decision to treat GO holders as unsecured is a "step in the wrong direction," the BDA said. "If ultimately accepted by the bankruptcy court, this treatment has national implications for general obligation bonds," the group said. "Full faith and credit general obligation bonds are a lifeblood for meeting state and local government financing needs, and the pledge they represent should not become undermined by specific, localized bankruptcy cases."

The plan didn't just upset the muni market. Local Detroit media Friday was reporting that retirees were complaining about the proposed settlement, which would require them to give up cost-of-living adjustments and health care.

A national pension advocacy group also blasted the plan.

"Gov. Rick Snyder and Kevyn Orr might consider this blueprint a 'comeback' and 'the best path forward,' but don't believe the hype," said Jordan Marks, executive director of the National Public Pension Coalition. "A more than 30% cut combined with the virtual elimination of health care is devastating to the people who dedicated a career to Detroit. Wall Street, which posted record profits in 2013, can afford to pay for the damage it reaped on the city."

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