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Moody's: Detroit GO Litigation Unlikely to Have National Legal Implications for GO Debt.

New York, March 11, 2014 — The bankruptcy litigation surrounding Detroit's general obligation bonds is unlikely to have a broad legal impact on the meaning of the GO pledges in bonds nationwide, says Moody's Investors Service in a new report. Moody's notes the Detroit parties may reach a settlement, the outcome of the Detroit litigation is unclear, and any bankruptcy court ruling would not be binding in other jurisdictions.

"Definitive statements about how Detroit's treatment of GOs would reshape the municipal finance landscape are premature," says Analyst Dan Seymour in the report "All GO Pledges Are Not Created Equal: Detroit Case Unlikely to Set National Precedent."

Under dispute is whether Detroit's unlimited tax GO debt is secured or unsecured, a key distinction in the federal Bankruptcy Code. The city wants to treat all its GO debt as unsecured, proposing a 20% recovery for GO bondholders that is significantly lower than the historical average on defaulted GO debt.

The parties can still reach a settlement with terms that depart from the city's proposal. Whether Detroit wins or loses the case, it would probably be appealed.

"The ultimate treatment of Detroit's GO pledge, once litigated, could turn out quite differently from what the city proposed," says Moody's Seymour.

Regardless of the outcome, the Detroit case will not provide broad clarity on the meaning of the GO pledge for three reasons: GO pledges vary widely across the US, few governments test their GO pledges because so few ever become distressed, and if there is a ruling unfavorable to bondholders, it will not be binding in other jurisdictions. Fundamental economic and financial strength, as Moody's discusses in its recently published GO rating methodology, will remain the primary drivers of municipal credit.

The Detroit case, however, is likely to guide the interpretation of GO debt for Michigan local governments in bankruptcy, an important outcome given the large number of distressed local governments in the state. The outcome will probably influence court cases outside Michigan as well, given the infrequency of litigation about GO debt.

It will also likely affect issuer and investor behavior inside and outside Michigan.

For more information, Moody's research subscribers can access this report at:

https://www.moodys.com/research/All-GO-Pledges-Are-Not-Created-Equal-Detroit-Case-Unlikely–PBM_PBM165551.

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