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With Bankruptcy Ending, Detroit Hears Warnings Not to Make Same Mistakes.

DETROIT—The judge who approved the city of Detroit's debt-slashing plan Friday warned officials not to make some of the same missteps that led to the nation's largest municipal bankruptcy case.

"What happened in Detroit must never happen again," U.S. Bankruptcy Judge Steven Rhodes said in a federal courtroom in downtown Detroit.

In his closing remarks after delivering a two-hour-plus oral opinion, Judge Rhodes made direct pleas to Michigan's governor, organized labor, city officials and the 688,000 people who call Detroit home. Judge Rhodes is expected to hold a hearing next week to set in place the final details of ending the bankruptcy case, including review of more than $140 million in fees.

The judge in his remarks Friday called on Michigan's governor to appoint highly qualified officials to a new financial oversight commission over the city's balance sheet. Judge Rhodes also expressed sharp concern about a potential conflict of interest on the commission, which allows the city's mayor and city council president to appoint themselves to the nine-member board.

But afterward, Detroit Mayor Mike Duggan defended the move, saying it had been approved by the state legislature and didn't pose a risk to the implementation of the city's restructuring plan. "He's going to find those concerns misplaced," the mayor said of the judge's misgivings.

The confirmation of the city's massive restructuring plan came more than 15 months after the city filed for Chapter 9 bankruptcy protection amid population loss, spiraling debt, and rising pension and health-care costs that forced the city into insolvency. The city earlier reached settlements with all of its major creditors. Some smaller creditors are still holding out and may appeal.

Relying on settlements that affect more than 100,000 creditors, the city's complex financial restructuring plan is legally reasonable, fair and equitable, the judge ruled.

He also said he heard and saw the deep anger and resentment of Detroit residents who felt as though their democratic rights had been trampled by a governor-appointed emergency manager who put the city into bankruptcy court in July 2013.

"I heard you. I urge you not to forget your anger," Judge Rhodes said, adding that anger should be transformed into constructive energy to help the city thrive again.

"We give it back to you with a fresh start," he told the city's elected leaders. "We hope we helped."

The city's restructuring road map calls for trimming $7 billion, or more than one-third of Detroit's estimated long-term debt, from its balance sheet. It was a rare milestone decision for cash-strapped cities, even among those that have sought bankruptcy protection.

The ruling however won't translate into a completely independent city. For at least the next dozen years, a new financial-oversight board will monitor the city's finances, with others watching its pension-fund investments.

"To put it simply, Detroit has a bright future," Republican Michigan Gov. Rick Snyder said at a news conference following the ruling. But "we have more work to be done" to improve the quality of life in the city.

Under the governor's direction, the city sought Chapter 9 bankruptcy protection on July 18, 2013, marking the nation's largest such filing. With the approval of the city's restructuring plan, Judge Rhodes is likely to issue a confirmation order within weeks, freeing the city from bankruptcy court.

Detroit's bankruptcy filing initially roiled unions and some financial groups after the city attempted to cut pensions sharply and restructure its municipal debt. But unions and pension groups dropped their legal fight after foundations and the state of Michigan stepped in to help make up shortfalls.

"While it has been a fast-track process through bankruptcy, it has not been painless," the city's pension trustees for police and firefighters said in a statement Friday. "It was an emotional, frustrating and expensive process that will help the city of Detroit shed billions in debt."

When Detroit made its bankruptcy filing, there were some concerns that banks and municipal bond investors might be reluctant to keep extending credit to shaky cities if Detroit was able to get out of certain deals that are generally considered rock solid in the financial world. But settlements with banks and bond insurers failed to upend the nation's $3.7 trillion municipal-bond market and significantly impair financing for other U.S. states and cities.

Still, some argue that Detroit could have trouble borrowing in the future, while others say the overall cost of municipal borrowing could grow since pension holders got a better deal than unsecured bondholders.

"Pension benefits were impaired, but recovery was higher than most other unsecured creditors," Moody's said in a report Friday. "The widely disparate treatment for unsecured creditors…leaves investors with more questions than answers for future bankruptcy cases."

The rating agency said that with the "absence of clear court opinions on the strength of each pledge, investors will therefore be more likely to negotiate with distressed cities in the future."

Municipal bankruptcies are still rare, and Detroit's trip through court was especially speedy. Late last month, the federal judge overseeing the two-year-long bankruptcy of Stockton, Calif., ruled that the distressed city can exit court protection without deeper cuts to its pension obligations.

Skeptics of the city's ride through bankruptcy court over 15 months say the exit plan doesn't ensure residents will return to Detroit or businesses will thrive.

"The Chapter 9 route has proven costly for Detroit, as it has for so many others, and its effectiveness at righting its ship upon emergence from bankruptcy remains in question," Standard & Poor's analyst Jane Ridley wrote Friday. "As Detroit enters postbankruptcy, it will be challenged to generate cost savings through operational restructuring while addressing a backlog of infrastructure and other needs."

She added that it will "still likely be difficult for the city to continue making the kinds of changes that will lead to the cost savings it needs to be operationally balanced."

On the plus side for advocates in the Detroit case, the bankruptcy plan scrapes roughly $7 billion of debt off the city's books but largely protects pensions, while reinvesting $1.7 billion in long-neglected city services.

One of the Detroit's most valuable assets, Detroit Institute of Arts, is leaving city hands, placed essentially into a separate trust through pledges equivalent to $816 million from foundations, corporations and the state of Michigan in an agreement known as the grand bargain.

The city's remaining debt load makes for little room for missteps, according to the court-appointed expert who cautiously endorsed the plan. The city's plan calls for borrowing $275 million in exit financing.

In the city's first months under bankruptcy protection, Mr. Orr proposed sharp cuts to city creditors. He wouldn't rule out asset sales, including the city-owned DIA. He said pension holders wouldn't be protected by state constitutional pension guarantees, and other bondholders could get as little as 10% of what the city owed them.

In the end, many creditors fared much better. Pension holders could see almost a full recovery under some scenarios, while some bondholders are expected to receive as much as 75% of the amount due.

Bond insurers hit the hardest settled for a combination of cash and city real- estate options that turned them from opponents of the city's reinvestment plan into partners in the city's renewal.

Since its bankruptcy filing, the city has shown signs of improvement, but enormous challenges remain. The city remains one of the nation's poorest and most unsafe. Neighborhoods outside Detroit's central core are beset by joblessness, unused vacant land and underperforming schools.

About 10 miles northwest of the federal courthouse where the city's future was mapped out, Ronda Morrison said she was both optimistic and cautious about what the years ahead held for her city. A lifelong Detroiter, Ms. Morrison inherited her father's shoe repair business and was determined to keep it going on Livernois Avenue, despite moving herself from her neighborhood home in north Detroit to downtown three years ago over safety concerns.

"We have two Detroits here. One works, and one doesn't," she said of the divide between a revived downtown and struggling outer neighborhoods. "I know we'll be turning around when you can feel it everywhere."

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