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Muni Bond Investors Beware: 'Staged' Bond Defaults Are Back.

At first it seemed like we were starting off the new year on a happy note. Five bond defaults as of the first day of the year that were immediately remedied by a bond call at full value, plus 1%, payable on the last day of the month.

Having been around the horn, however, it seems more to me that “staged defaults” in municipal bonds are back. Such defaults are the bane of the municipal bond market since they are generally motivated by a desire to get out of a high coupon bond that has no early call provision. We saw a wave of such defaults in the 1980s as we came down from the high rates back then and I suppose, with the benefit of 20/20 hindsight, we can expect quite a few in 2020.

I was struck by the January 10, 2020 announcement by the Huntington National Bank that five of the bond issues it is trustee for, had not made their interest payments to the bank and therefore, the January 2 interest payment to bondholders would not be made. The bonds were thus declared in default. This was followed by a second letter from the trustee, dated the same day, advising that all the bonds from the five issues were being called by the obligor on January 31, 2020 at par plus a 1% premium plus accrued interest.

A call to the Huntington National Bank was not returned. I then turned to a recipient of the January 1 notice letter, Waldrep Law, which describes itself as “a boutique law firm specializing in business bankruptcy, healthcare restructuring and insolvency, and long-term care. We offer a unique combination of top-tier credentials and efficient, individualized client service.” As soon as I identified myself and why I was calling, I received a “no comment” and a hang-up. I then called Tortoise Credit Strategies LLC, a firm that represents itself as a “Bondholder Representative.” No call back from them either. I suspect they hold these bonds for investor clients.

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by Richard Lehmann

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