Federal judge to review objections to Detroit bankruptcy filing

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Legal representatives of various Detroit creditors, as well as individual residents including city workers and retirees, filed close to 100 objections to the city's impending bankruptcy on Monday, the deadline for objection filings. A hearing to determine the ultimate eligibility of Detroit to proceed with the largest municipal bankruptcy filing in US history is set to begin October 23.

The bankruptcy filed last month by Emergency Manager Kevyn Orr—whose former law firm Jones Day represents some of the biggest Wall Street banks—is aimed at forcing through deep cuts in workers' pensions and restructuring the city in the interests of the wealthy.

Two of the city's largest creditors are the Police and Fire Retirement System and the General Retirement System, which fund the pensions and health benefits of some 31,000 current and retired city workers. Representatives of the two groups contested Orr's claim that the pension systems, with about $5 billion in total liability, are underfunded by $3.5 billion, a figure based on various conjectures of future growth. They provide their own figure of just $644 million in unfunded liabilities.

The pension groups met with Orr's deputies for three hours on Monday before filing a joint objection, calling the bankruptcy "illegal, unconstitutional and erroneous." Michigan's state constitution explicitly protects public pensions as "contractual obligations" which "shall not be diminished or impaired," but Orr has argued that federal bankruptcy law overrides this state-level protection.

In order for Detroit to qualify for bankruptcy under Chapter 9, Orr must show the city is insolvent, that he has the permission of the state to proceed, and that he either has negotiated with Detroit's creditors in good faith or that it is no longer practical to do so.

Legal experts doubt whether appeals based on the constitutionality of potential cuts to pensions will carry any water with federal judge Steven Rhodes, who is presiding over the bankruptcy proceedings, since merely entering into bankruptcy does not necessarily imply cuts to pensions. Orr has lumped pensions in with other "unsecured" debt, such as general obligation bonds, and threatened to slash them all by up to 90 percent. However, official details of the debt-cutting plan, including the fate of the pensions, conveniently do not have to be submitted until a March 2014 deadline.

Also objecting are AFSCME (American Federation of State, County and Municipal Employees) and the United Auto Workers, each on the grounds that Orr did not negotiate with them in good faith. AFSCME attorneys said Orr was "seeking the haven of bankruptcy to illegally attempt to slash pensions." A UAW lawyer called the bankruptcy filing "a blunt instrument to force retirees and pension-vested workers into negotiating away their benefits."

The unions are not at all opposed to imposing deep cuts on the workers they claim to represent. They simply want to remain a well-compensated part of the process.

In an August 14 interview, UAW president Bob King told *In These Times* magazine, "The UAW is strongly opposed to the bankruptcy, especially because city leaders made no effort to sit down with municipal workers and see if all parties concerned could work together, make cutbacks and address the crisis before taking this step." What "cutbacks" did King have in mind? "If we restructure the city just like we restructured the auto industry, there's hope that Detroit, too, can see a turnaround," he said.

The restructuring of the auto industry in 2009, to which King refers, consisted of the slashing of wages of new hires by 50 percent, the effective elimination of the eight-hour day and of overtime and weekend pay via the "alternative work schedule," the cutting of pensions and benefits, and the destruction of tens of thousands of jobs. In exchange for helping to impose a record reduction in labor costs, the UAW was given billions of dollars in stock by the auto companies, securing the interests of the UAW apparatus as the automakers generated $11 billion in 2012 profits.

King declared that the “Detroit branch of the AFSCME drafted and proposed a $180 million savings package” and that AFSCME “met with the UAW about this, and we agreed that the unions should collaborate with the city and try to make these savings happen.” Instead, he complained, “city leaders, for their part, didn’t even bother responding to the AFSCME’s plan. They ignored it and filed for bankruptcy.”

AFSCME attorneys also insisted in their objection that Orr failed to have certain unspecified city assets appraised for sale until after the filing, which would mean he couldn’t really have known whether the city was insolvent at the time. They are doubtless referring to recent revelations that Orr has hired Christie’s auction house to appraise works of art at the Detroit Institute of Arts (DIA), Detroit’s world-class public arts museum.

The juxtaposition of the sale of public artwork to the gutting of pensions is fictional. If Orr and the financial elite whom he represents have their way, they will rob from Peter as well as Paul, selling Detroit’s art and cutting workers’ pensions at the same time.

For his part, DIA chairman Eugene A. Gargaro—a former corporate executive—made an unprincipled and craven statement over the weekend, declaring that the museum “support[s] Kevyn Orr’s goal of rebuilding the City through strengthening of the City’s institutions and governance” and would not be filing an objection to the bankruptcy. While declaring that the museum would go to court to prevent the sale of its collection, the statement grotesquely wished Orr success and urged him not to undermine his supposedly legitimate goals by “jeopardizing Detroit’s most important cultural institution and the economic, educational and other significant benefits it brings to the city and the region.”

Other objections came through handwritten letters from individual residents, as well as the signing by about 20 residents of form-letters prepared by erstwhile mayoral candidate Krystal Crittendon, herself a former corporate lawyer for the city, and Reverend Charles Williams II of Al Sharpton’s race-based National Action Network (NAN). The letter meekly objected on the procedural grounds that not enough time was given for Detroiters to object to the bankruptcy. “We have to make sure we are following the law,” said Crittendon. Prior to the bankruptcy judge’s deadline many analysts expected that there would be objections from the city’s biggest bondholders, including BlackRock Financial Management Inc. and Nuveen Asset Management LLC, and bond insurers such as New York-based Assured Guaranty Ltd. and National Public Finance Guarantee Corp. However, none of the bondholders and insurers filed a challenge to the bankruptcy.

The bond insurers—which make payments for the city when it cannot meet its financial obligations—are particularly at risk of losses, since Orr has characterized tax-funded general obligation (GO) bonds—long considered secured debt and a priority for repayment during bankruptcy proceedings—as “unsecured debt.” In this way, he is lumping GO bonds with the city’s pension and health care obligations, offering only pennies on the dollar in payment.

Orr’s move to change the status of the city’s debt is shaking up the nearly $4 trillion municipal bond market in the US. In the future only the largest hedge funds and Wall Street banks will take on the risk, driving up borrowing costs for distressed cities across the country and paving the way for the gutting of pensions and other benefits owed to millions of city workers across the US.

Patrick Darby, a bankruptcy attorney at Bradley Arant Boult Cummings LLP, told Reuters bond creditors may have concluded there are no other alternatives for Detroit but bankruptcy. “As the bankruptcy proceeds, bondholders will vie against pension funds and other creditors for payment from the city,” Reuters wrote.

In addition to being insured, the big bondholders are also looking for a favorable ruling from the bankruptcy judge. Richard Ciccarone, a managing director at McDonnell Investment Management, told Reuters bond creditors may believe the Chapter 9 bankruptcy proceeding will give them a chance to argue the city must honor the security provisions in Detroit’s debt. “The chance for 100 percent payment (for unlimited tax GO bonds) still exists—if not on time, over time,” Ciccarone said.