Bankruptcy judge tells Detroit officials to renegotiate bank swap deal

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US Bankruptcy Court Judge Steven Rhodes rejected a deal Thursday that would have seen the city pay $169.2 million to Bank of America and UBS as a termination fee for the catastrophic 2005-2006 interest rate swaps deal the banks foisted on the city.

Rhodes acknowledged that the city was "likely to succeed" if it challenged the legality of the swaps deal on the grounds that it violated the state's Gaming Act and Public Act 34 (Revised Municipal Finance Act of 2001). The former specifies a list of "socially useful" purposes to be funded by gambling revenues, while the latter protects municipalities from predatory financial arrangements.

Nevertheless, the judge advised Detroit Emergency Manager Kevyn Orr to pay the banks anyway, albeit at a lower level.

"It [the court] must conclude that the $169 million settlement to swap counter parties is just too high a price to pay for the city to put the issue behind it," Rhodes said. The judge was at pains, however, to emphasize he would have approved the deal if only the termination fee had been smaller.

Rhodes endorsed the specious claim by Orr and Jones Day lawyers who crafted the payoff deal, saying litigation would be pose significant "complexity." He recommended that the city and the banks seek a negotiated solution. In so doing, he gave his imprimatur to the payoff of the same banks that had swindled the city.

"The court must emphasize that the parties should not interpret the court's denial of this particular settlement to mean that they should not continue to resolve these issues through negotiations," Rhodes said. "They absolutely should. The settlement of the swaps claims is better than litigation. If the city pursues immediate litigation, so be it, but negotiation should be pursued at the same time. The court strongly encourages the parties to continue to negotiate."

Rhodes did not and could not rebut the arguments of Ambac Assurance attorney Caroline English, who said on Monday, "This deal should have the swap counterparties paying the city, not the city paying the swap counterparties." Rhodes argued that the task before the court was to decide on the $169 million payment to the banks, not to judge the legality of the swaps deal.

The hypocrisy is glaring. Instead of ruling on the clear violation of the law—which would raise the issue of criminal prosecution and ordering the banks to pay reparations—the judge advised the city to pay the banks. Clearly aware of the anger building in the working class against the entire bankruptcy process, he calculated that lowering the figure paid to the banks would make the deal more palatable to the public.

The swaps deal—under which Detroit has been forced to make annual interest payments of $50 million to Bank of America and UBS for years—goes to the heart of the financial interests that are gaining from the impoverishment of the city's 23,500 retirees and the looting of the artwork of the Detroit Institute of Arts (DIA).

Under Orr's original plan, the city would have paid $230 million--80 percent of what the banks were demanding—to end the swaps deal. Meanwhile, pension funds are being offered 16 cents on the dollar. Orr and Jones Day renegotiated the deal down to $169 million in mediation sessions with Judge Gerald Rosen.

Before Orr releases his "adjustment" plan to restructure the city on behalf of the banks and big business, the judge is seeking to craft some sort of negotiated settlement with all parties, including cutting a deal with the trade union bureaucracy to push through massive cuts in pensions, wages and health benefits.

In pursuit of this, a group of nine wealthy philanthropic foundations, including the Ford Foundation, the Kresge Foundation, and the John S. and James L. Knight Foundation, has been working on an agreement that would supply a limited amount of funds. Rosen and the media are claiming that this would “save” city worker pensions and the DIA. On Thursday, it was reported that Governor Rick Snyder had become involved in these efforts.

The money from the foundations—valued at $330 million spread over 20 years—is only a fraction of the billions that would be required to meet pension obligations, according to numbers put forward by Orr. The judge is calculating, however, that it may enough to firm up the support of the trade union apparatus, which is concerned not with the pension and heath benefits of retirees, but with maintaining control of multi-billion-dollar pension fund investments.

The purpose of this “rescue” package is the same as that of Rhodes' move to temporarily block payment to the banks. Like Rhodes, Snyder and the trustees at the elite foundations are conscious that rage is building against the further enrichment of the banks on the backs of Detroit pensioners.

Whatever the specifics of such a deal, the pensions will be slashed and the century-long public ownership of the DIA and its priceless collection will be ended.

Throughout the trial, Rhodes has sought to cultivate the appearance of a wise, neutral arbiter, carefully considering the rights of the city and its residents.

Nevertheless, he has shown by his rulings that he regards the financial and political elite as being above the law. By approving the bankruptcy, Rhodes effectively upheld Public Act 436, the authoritarian emergency manager law that granted Orr the power to throw the city into bankruptcy and tear up pensions, in violation of the Michigan state Constitution. Now, faced with clear evidence that the banks have committed financial crimes, Rhodes has upheld the right of these institutions to plunder cities with impunity.

"The court must insist that any settlement be rational," Rhodes said near the end of his ruling.

Any deal that hands over more money to the banks is irrational. A truly rational settlement would force the banks to pay hundreds of millions in reparations to the people of Detroit and would bring criminal charges against the executives of the firms that swindled the city.

That will not be carried out by the courts, which are not neutral arbiters, but tools of the financial oligarchy. Holding the financial criminals accountable and impounding their ill-gotten gains for the benefit of the people is the task of a politically conscious movement of the working class.

To conduct this fight workers must know the truth. That is why the Socialist Equality Party is holding the February 15 Workers Inquiry into the Bankruptcy of Detroit and the Attack on the DIA and Pensions.