

Detroit Unions, Retirees Face Battle to Kill Bankruptcy

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Snyder is being called as a witness by the United Auto Workers union, which represents some city workers and is trying to show that the bankruptcy filing wasn't in good faith. Photographer: Scott Eells/Bloomberg

Detroit's unions and retired workers face longer odds of ending the record-setting bankruptcy than the city does of winning continued court protection in a trial that started today, lawyers not involved in the case say.

At a trial that may last into next week, opponents will attack the decision by a state-appointed emergency manager to put Detroit into bankruptcy, where creditors can't try to seize assets or file suits that disrupt city reorganization efforts.

Creditors have lost four of five court battles mounted since 2008 to strip municipalities of bankruptcy protection. Detroit also is armed with a "mountain of evidence" showing that it's entitled to federal bankruptcy protection, Bruce Bennett, a lawyer for the city with Jones Day, told U.S. Bankruptcy Judge Steven Rhodes at the start of the trial.

"Detroit is bankrupt in every sense of the word, including legally," Lee Bogdanoff, who represents Jefferson County, Alabama, in its bankruptcy case, said yesterday in an interview. "The Detroit tragedy is

precisely what Chapter 9 is designed to address, in a single federal forum.”

The city must show that it is insolvent, is entitled under state law to file for bankruptcy, that it tried to negotiate with creditors or was unable to do so, and that it intends to file a plan to adjust its debts.

Basic Services

Detroit is “failing to provide basic services,” Bennett said. Rhodes also faces another consideration that isn’t among the tests laid out in the bankruptcy code, said Larry Dubin, a professor at the University of Detroit Mercy School of Law.

“If the bankruptcy was called off, it seems like there would be a ton of litigation that would be filed against the city,” Dubin said.

Once Detroit lays out its evidence, the burden will shift to the unions and retirees to show why the city is wrong, bankruptcy attorney James E. Spiotto, a partner with Chapman & Cutler LLP, said in an interview.

Two key attacks on the bankruptcy filing involve constitutional challenges that will either fail to convince the judge or can be put off until later in the case, Spiotto said.

“We think we should win,” said Sharon Levine, a partner at the law firm Lowenstein Sandler PC who is representing one of Detroit’s biggest unions, the American Federation of State, County and Municipal Employees.

Protected Rights

“We understand that the judge is concerned about Detroit’s financial situation,” she said. “The pensioners here, particularly in Michigan, have a real constitutional right not to have their pensions diminished. Those rights are protected by the federal and state constitutions.”

Should the unions and retirees lose, “all options are open,” including an appeal, Levine said.

In July the city filed the biggest U.S. municipal bankruptcy with about \$18 billion in debt, saying it didn’t have the money to pay its bondholders, retirees and employees all it owes them and still provide basic services to citizens.

Unions, retirees and the city’s pension system claim Michigan’s constitution prevents Detroit from reducing worker pensions. They make the same argument about the law authorizing emergency manager Kevyn Orr to file the bankruptcy.

Rhodes challenged the assertion that the state constitution bars any cuts to municipal retiree payments, in or out of bankruptcy.

Pension Priority

Union and retiree lawyers have said that even proposing the cuts makes a Michigan city ineligible for bankruptcy protection. When an attorney for the city's pension system, Robert Gordon, argued that pension payments get priority over other kinds of debt, including bonds, the judge interrupted him.

"That violates the bankruptcy code," Rhodes said. Similar debts must be treated the same under federal law, he said.

Governor Rick Snyder, who testified under oath in a videotaped deposition earlier this month, is prepared to testify in court Oct. 28, said Matthew Schneider, a lawyer with the state. Snyder is being called as a witness by the United Auto Workers union, which represents some city workers and is trying to show that the bankruptcy filing wasn't in good faith.

Bennett said today that the city negotiated in good faith, answering questions it was asked by creditors in talks in June and July and trying, and failing, to persuade unions to present a counter-proposal. Holding talks with all bondholders was impractical because there were so many, and cutting bond debt outside of bankruptcy would have required agreement from 100 percent of them, he said.

Conspiracy Alleged

Jennifer K. Green, an attorney for a city pension system fighting the bankruptcy, said Detroit officials were never serious about trying to fix the city's finances outside of court. State officials conspired with Jones Day, Bennett's firm, to create a new emergency manager law and use to file a bankruptcy that gives the city leverage over unions and retirees, she said.

If the city wins the trial, any appeal would first go to the U.S. District Court in Detroit, where a judge would review the record of the trial and other evidence. The bankruptcy case would continue, unless opponents could convince a judge they have a good chance of winning the appeal and they face an imminent threat.

Appealing all the way to the U.S. Supreme Court would be difficult, said R. Dale Ginter, a bankruptcy lawyer at Downey Brand LLP in Sacramento, California.

Rhodes has insisted that all testimony and other evidence be presented in the five days he has scheduled for the eligibility trial. He said he preferred live testimony to written excerpts of witness statements.

Record Building

That shows that the judge is being careful to build a record that will be difficult to defeat on appeal, Ginter said.

Bankruptcy critics may allege that Detroit isn't truly insolvent by challenging the claim that the city's pension systems are underfunded by \$3.5 billion.

Because the city's finances are so clearly in crisis, that argument will be hard to win, said Ginter, who represented retired workers in the bankruptcy case of Vallejo, California.

"If you throw the city out of bankruptcy, what does it do?" Ginter said. "Who's going to get paid? There simply is not enough money."

The case is City of Detroit, 13-bk-53846, U.S. Bankruptcy Court, Eastern District of Michigan (Detroit).

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