Call on the Detroit City Council to Reject Emergency Manager Order #17 - "Approval of Post Petition Financing"

The Detroit city council has a crucially important decision to make: Accept the proposed $350 million Debtor in Possession (DIP) deal with Barclays Capital to pay off the termination fees on swaps with Bank of America and UBS, or reject the deal and offer a counter proposal. *We urge the council to reject the deal for the following reasons:*

This agreement would set a dangerous precedent.

The DIP deal Kevyn Orr, the city's Emergency Manager appointed by Governor Rick Snyder, has worked out with Barclay's is an unprecedented move in a municipal bankruptcy – Bond Buyer calls it the "first deal of its kind"[i]- and would set a dangerous precedent for municipal bankruptcies in the U.S., essentially allowing wealthy big banks to jump to the front of the creditors line while retired seniors are facing drastic cuts in the retirement income they depend on. That's exactly what the banks want – to use Detroit to set precedent and change the way municipal bankruptcies work so that they are structured more like corporate bankruptcies. Municipal finance experts and the financial press are starting to scrutinize the proposed deal and are raising this point. For example, Matt Fabian, managing director at Municipal Market Advisors, is quoted in an October 16th Bond Buyer article saying "The state and the restructuring community wants this kind of financing to work so as to facilitate future bankruptcies…The state is doing what it can to make sure DIP lenders are protected and repaid." [ii]Detroit is a city with citizens who depend on elected officials to make decisions in their best interest, and we can't let the Governor Snyder's appointed Emergency Manager, Kevyn Orr, prioritize the interests of banks instead.

Wall Street's Swaps have already cost the city unnecessary millions.

Since 2008 alone, Detroit has sent nearly $800 million in unnecessary payments to Wall Street banks, including a $550 million payout just last year. Now Barclays stands to profit from its role in a deal to pay off Bank of America and UBS first. This deal is giveaway to the same banks that helped get Detroit into this mess in the first place. Under this deal, the Barclays loan is secured with income tax and casino tax revenue, and net cash proceeds from the possible sale or lease of city assets exceeding $10 million. Even the financial press has noticed how unreasonably generous the terms of the loans are to the bank. The loan repayments would have priority over all other post-petition claims, and pre-petition unsecured claims, according to an analysis by Crain's. [iii] And, in addition to an undisclosed "commitment fee" Barclays would get, the loan carries an interest rate based on the London Interbank Offered Rate plus 2.5%, plus a 1% LIBOR floor, translating into an effective rate of 3.5%. If the city defaults, the spread rises by another 200 basis points. Bond Buyer quotes Robert Miller, senior portfolio manager for Wells Capital Management, describing these terms as "pretty rich," and "a pretty big number…The 3.5% interest rate "represents a hefty premium over the two-year Treasury yield, which closed yesterday at a mere 0.35%,"[iv] .

Right now, the existing swaps are a "soft" liability- meaning the city doesn't have to pay the fair market value of the swaps right now. Orr wants to turn that into a hard dollar settlement with the banks at a time when the swap liabilities could, with possible interest rate changes, actually start to decline. [v]This makes absolutely no sense, unless you look at it from the bank's point of view and are concerned only with the bank's bottom line.

This deal also puts Detroit in a very vulnerable position, with terms that leave Barclays far too much control and power. From Bond Buyer:

> "The deal includes a so-called lockbox structure, where the casino and income tax revenues will flow first into a bank account controlled by Barclays. In the event of a default, $4 million of each revenue stream will be set aside, and the city can continue to access the rest. The term sheet features a lengthy list of events of default. If the city ceases to be under the control of an emergency manager for 30 days, for example, it would be

considered a default unless Barclays determines that a transition advisory board or consent agreement ensure continued financial responsibility."[vi]

The Emergency Manager's plan is a clear effort to help the banks get around bankruptcy Judge Steven Rhodes' August 2013 ruling on secured debt:

In August, the Detroit bankruptcy judge, Steven Rhodes, invalidated an earlier agreement that would have secured casino revenue to pay the banks. After years of profiting from badly structured financial deals and helping force the city into insolvency, bankers had forced Detroit to agree to give them a guaranteed cut of city revenue from casinos-essentially allowing banks to jump the creditors' line by treating the swaps as "super senior" debt. When the bankruptcy judge recently ruled that these banks had wait in line just like the rest of the people in Detroit, the bankers worked out a special deal with Kevyn Orr, whose former law firm, Jones Day, represents Bank of America, JP Morgan Chase, Wells Fargo, Citigroup and numerous other major Wall Street players. According to Bond Buyer, it was Jones Day and the city's investment banker, Miller Buckfire & Co who led the effort to secure the DIP financing.[vii] We should be asking them to explain why, who they think this benefits.

As our elected officials you are morally, ethically and legally responsible for protecting the rights and needs of the residents of Detroit.

Banks must be made to pay for the mess they created and profited from, rather than be rewarded with a place at the front of the line. Workers and citizens in Detroit have already suffered service and job cuts and pay and benefit decreases. **It's time to stand up for the people of Detroit against bullying banks.** We should be negotiating with the banks to release Detroit from the bad swap deals without termination fees, not taking out expensive loans to pay them off. Reject this deal and keep this $350 million in Detroit, where it is it most needed.

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[i] http://www.bondbuyer.com/issues/122_198/detroit-wins-350m-dip-loan-from-barclays-1056450-1.html
[ii] http://www.bondbuyer.com/issues/122_200/detroits-dip-deal-could-pave-way-for-bankrupt-financing-1056553-1.html
[iii] http://www.crainsdetroit.com/article/20131011/NEWS/131019959/#
[iv] http://www.bondbuyer.com/issues/122_200/detroits-dip-deal-could-pave-way-for-bankrupt-financing-1056553-1.html
[v] http://www.bondbuyer.com/issues/122_200/detroits-dip-deal-could-pave-way-for-bankrupt-financing-1056553-1.html
[vi] http://www.bondbuyer.com/issues/122_200/detroits-dip-deal-could-pave-way-for-bankrupt-financing-1056553-1.html
[vii] http://www.bondbuyer.com/issues/122_198/detroit-wins-350m-dip-loan-from-barclays-1056450-1.html