

# From a doodle to the Grand Bargain

## How the bankruptcy in Detroit was resolved through mediation

By Hon. Steven W. Rhodes, Retired Chief Judge, U.S. Bankruptcy Court for the Eastern District of Michigan and Hon. Gerald E. Rosen, Retired Chief Judge, U.S. District Court for the Eastern District of Michigan



RHODES



ROSEN

**Judge Rhodes:** Detroit's problems were well known long before it filed bankruptcy in July 2013. Because it was insolvent, its municipal services were inadequate and its government was under state control. Its residents and its business were suffering from outrageous response times for police, fire and emergency medical services, a failed street lighting system, widespread blight, unreliable public transportation, growing legacy obligations and a shrinking tax base.

These problems could only worsen with time. Time was therefore the enemy. Detroit's fresh start would depend on the prompt confirmation of a feasible plan. Originally, my goal was to confirm a plan — a plan that would restore adequate city services — within one year after the bankruptcy filing.

But there was a major obstacle to this goal — litigation. It was easy to foresee that litigation over the contentious and complex issues in the case would make it impossible to resolve it within one year — or three, or even five years — and the city would continue to be at war with its police, firefighters, unions, retirees, vendors and financial creditors.

The only way to overcome this obstacle was successful mediation. The deliverable for mediation would be a confirmable plan of adjustment.

Mediation was also important because, as an ongoing enterprise, Detroit would need to restore its relationships with all of its constituents, including its creditors, which only mediation could facilitate. A litigated result, while legally possible, would further sour the city's relationships for years to come.

So, the Detroit bankruptcy case needed to be resolved through mediation.

Selecting the right mediator was therefore crucial. The work of the mediator would require the right combination of weight of office, love of the City of Detroit, connections, communication skills, thick skin, creativity and relentlessness. So, I recruited Judge Rosen to be the mediator because he possessed all of that.

It was the smartest thing I did in the case. Although my personal goal to confirm a plan within one year did slip, we came close — 16 months. Most of the credit for that prompt result goes to Judge Rosen, his extraordinary team of mediators, and the lawyers and professionals in the case. The result of their work in the mediation was a confirmable plan that every creditor class that came to the mediation table supported.

Thanks to mediation, Detroit is now two years into its fresh start. While its revitalization has a long way to go, it does have a strong beginning.

**Judge Rosen:** When Judge Rhodes asked me to be the mediator in the Detroit bankruptcy case, I knew that the city was sliding into oblivion after decades of financial and political dysfunction, dramatic population and revenue loss, a culture of corruption and an ingrained distrust between the city and its employees, retirees and creditors. This would become the backdrop against which Judge Rhodes and I would navigate the legal and bargaining landscape in the case.

I often say that Judge Rhodes had the front room — handling the complex and novel legal issues in the courtroom, and I had the backroom — negotiating with the parties through the daunting maze of financial, legal and political issues while searching for a consensual resolution to this hydra-headed monster.

But the city had little revenue and almost no monetizable assets available to make deals with its creditors, with one exception. The city did own the world-renowned art collection housed in the crown jewel of the city's cultural life, the Detroit Institute of Arts. The collection is enormously valuable and the creditors wanted that value.

But this did not seem to be right for the city's future. It would be an exclamation point on a Detroit obituary that many were already writing. Also, liquidating the art would certainly result in many complex legal issues that would take years to resolve, as well as cultural, economic and political issues that might never be resolved.

But the needs of the city's creditors were real and human. Retirees' modest pensions and health benefits were threatened with drastic cuts that would leave many impoverished and reliant on a strained social services network. The city's employees had taken years of pay cuts.

Borrowing more money was not an option. The city was at, or beyond, its statutory borrowing limit and its financial credit rating was at junk status.

Many were presenting the preservation of the treasures of the DIA and addressing the needs of the city's retirees as a binary choice — one or the other.

But, after talking with the attorneys for the city and its creditors, an idea began to form. Why not see if we could bring in new money by leveraging the plights of both the DIA and the city's retirees?

So, one morning, I doodled the germ of an idea on the cardboard back of a legal pad. The idea evolved into what has become known as Detroit's Grand Bargain — an unprecedented marriage of state, philanthropic and private resources to assist the city and its retirees while preserving the art at the DIA. This marriage, in turn, created paths to additional agreements between the city and its other creditors.

Only mediation could have taken this doodled idea from the back of a legal pad to a confirmable and almost fully consensual plan of adjustment — and the doodle is now hanging in the DIA representing that resolution!

The mediation process in this case can be characterized by what I call the four "Cs":

**Candor:** Any successful mediation requires the parties' full candor. As Judge Rhodes is fond of saying, paraphrasing Mark Twain, "Denial is a river in Egypt." It is not a path to feasible agreements. Parties must be candid not only with their mediating partners, but with themselves. The bankruptcy mediators had many "full, frank and candid discussions" (as the

diplomats say) with the parties. These conversations were not easy, but eventually the parties began to see alternatives to their own positions.

**Cooperation:** Detroit's history with its creditors had created layers of scar tissue. To move forward, the mediators had to offer opportunities for the parties to vent. Only then could the mediators focus on the real issues and open paths to cooperation. As this cooperation grew, the parameters of agreements were revealed.

**Creativity:** When a mediation begins, it often seems that there are limited and finite avenues to resolution, avenues that are unpalatable to one side or the other, and sometimes to both sides. A mediator can help the parties begin to think beyond these boundaries to find creative solutions that might offer both sides a win. The Grand Bargain is but one example of a creative solution. There are many others in the case.

**Courage:** Sometimes, to get past self-interest and rigidity of thought, parties must find the courage to see that a result that is different than originally sought may unlock new opportunities. Many examples of personal courage stand out in the case, from the leaders of the retiree groups, to representatives of the city's unions, to the financial creditors and their attorneys and insurers, to visionary philanthropic leaders, to political leaders. For example, Shirley Lightsey, the president of the non-uniformed retiree association, facing strong opposition to Grand Bargain, created a pin that said, "You can't eat principles." Governor Rick Snyder had the courage to authorize the bankruptcy in the face of vehement opposition from Detroit and then also to ask the legislature to appropriate \$350 million for the Grand Bargain. Leaders of the foundation community had the courage to do what had never been done before — to come together and pool their resources to preserve both the city's pensions and its art. And Tim Coleman, representing some of the bond insurers, stepped up to lead the first settlement between the city and financial creditors.

The story of the mediation in the Detroit bankruptcy case is about more than just a series of deals and the resolution of a case. It is the story of the many heroes and heroines coming together in mediation to overcome doubt, distrust, rigidity, cynicism, self-interest and the ghosts of the city's past mistakes, and their own, to rescue and give rebirth to an iconic American city.

Detroit's bankruptcy case is a story about the power of mediation.

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*Gerald E. Rosen is a neutral for JAMS, and served as the chief judicial mediator for the Detroit bankruptcy case — the largest, most complex municipal bankruptcy in our nation's history — which resulted in an agreed upon, consensual plan of adjustment in just 16 months. He spent almost 27 years on the federal bench, including as chief judge, U.S. District Court for the Eastern District of Michigan. Prior to this, Judge Rosen was a senior partner in the law firm of Miller Canfield.*