

DETROIT'S BANKRUPTCY

The 1940's and 50's were Detroit's heyday. The city was a shining example of American success that attracted investment and laborers searching for blue-collar jobs tied to GM, Chevrolet and Chrysler. Detroit was the Motor City, the 5th largest city in the US with a population of approximately 2 million people with excellent geographic advantages in the center of a major manufacturing belt. On July 18th, 2013, the city of Detroit, nearly \$20 billion in debt, filed for bankruptcy, igniting a legal battle that is likely to drag on for years while adding millions in legal fees to the city's financial woes.

Like most problems, the signs of dysfunction have been accumulating, in Detroit's case, for decades. Since the

1967 race riots that started both businesses and middle-class families fleeing for the suburbs, Detroit has been in steady decline, in part due to mismanagement but also because the American automotive industry has failed to stay globally competitive. As the de-industrialization process restructured the US economy and car manufacturing moved to various cities both domestic and overseas, Detroit suffered for its lack of economic diversity. What was once America's manufacturing belt is now called by some the Rust Belt, underscoring the difficulty of maintaining blue-collar jobs in this part of the United States. Globalization has its winners and losers, and the city of Detroit, once a champion, is now on the ropes.

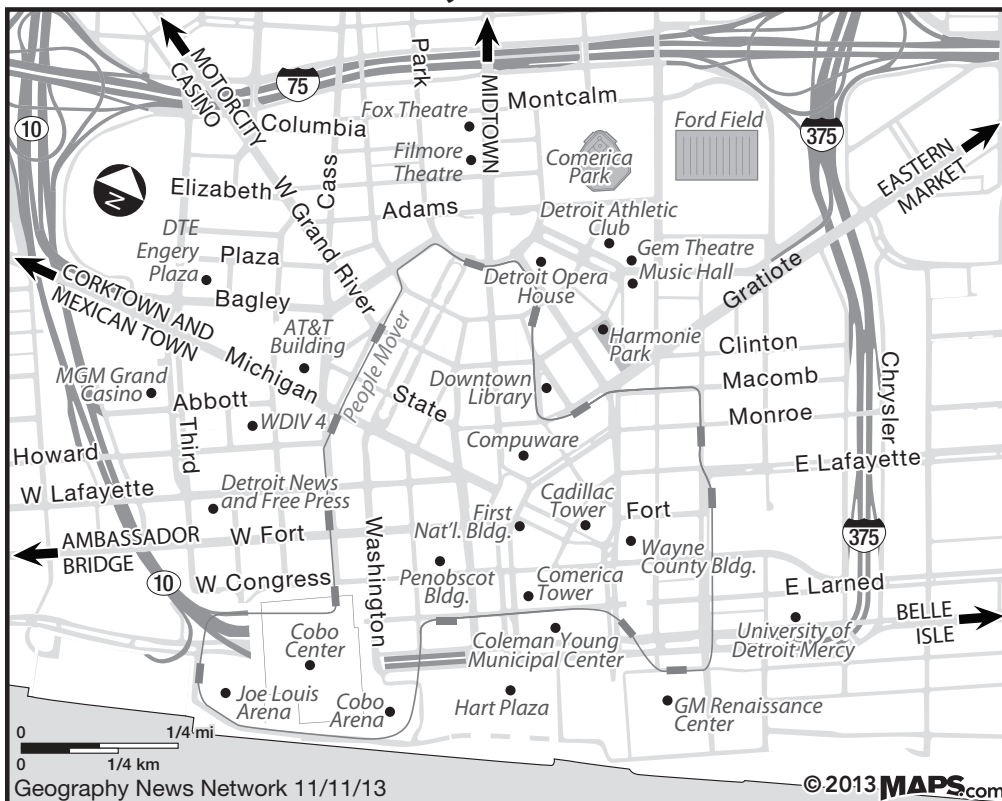
Detroit is the largest city to declare bankruptcy and more importantly the first major American city to essentially fail as a major metropolitan area. At 139 square miles, sections of the city are reminiscent of a post-apocalyptic bestselling novel: 80,000 buildings stand empty, 40% of the streetlights don't work, and it routinely takes police one hour to respond to a 911 call. With no fear of punishment, crime is on the rise and urban blight pushes

down property values. The population has shrunk to 700,000 citizens causing the tax base to continue to contract despite high city property taxes. City services are spread thin creating a cycle where poor services encourage more people to migrate elsewhere. It's estimated that half of the population over the age of 16 is unemployed although the official unemployment rate is 18.6%. Half of those who remain refuse to pay taxes and the city is too short handed to be able to enforce tax laws. In 2011, \$246.5 million in taxes went unpaid.

Detroit is not alone, but it is the most dramatic example in the United States of a city failing to provide sufficient jobs to sustain the local economy. Just like the automakers that made it famous, Detroit now looks to the federal government for a bail-out in the form of bankruptcy. Three months into the process, the legality of the bankruptcy is playing out in federal judge Steven Rhodes courtroom. State-appointed emergency manager Kevyn Orr believes bankruptcy is the only way to relieve the city's burden and allocate monies toward rebuilding the city's services and infrastructure. Detroit attorney Bruce Bennett claims that 65 cents of every tax dollar goes to paying liabilities, an untenable position for the city. But creditors, unions and municipal retirees oppose the Chapter Nine argument that would pay creditors pennies on the dollar and likely gut municipal pensions and health care that they say are protected by Michigan's Constitution. Mr. Orr argues that state law is superseded by federal bankruptcy law leaving many wondering who will protect the retirees, their pensions and a bond system that has rarely suffered losses.

In September, the White House announced it had allocated and, in some cases, reallocated up to \$300 million in grants for Detroit. Much of previous years' allocations were caught up in red tape due to the aforementioned city mismanagement. Now Washington is working to expedite the funds transfer process that would award specific amounts to blight removal, economic development, hiring more police and firemen, transportation and fixing the

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street lights.

There is no simple solution to the problems that Detroit is now facing. In such difficult economic times, both

unions and city workers nationwide will be watching to see how this bankruptcy plays out. If Detroit is successful in its bid for bankruptcy other cities may be tempted to follow suit and

slash benefits promised to municipal workers after a life time of work.

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QUESTIONS:

1. Should Detroit be allowed to file for bankruptcy? Who would benefit and who would suffer?
2. If Detroit is denied bankruptcy what can be done to sustain the city?
3. If Detroit successfully files for bankruptcy do you think other cities will follow suit?

SOURCES:

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