

# THE BOND BUYER

THE DAILY NEWSPAPER OF PUBLIC FINANCE

## Central Falls Pension Pacts a Boon for Bond Market

Tuesday, January 10, 2012

By [Paul Burton](#)

Bond lawyers and restructuring experts agreed that bankruptcy court approval of pension agreements between Central Falls, R.I., and its retirees and public sector unions is good for the bond market.

They also said it shows an effective use of Chapter 9, the bankruptcy vehicle for municipalities.

Judge Frank Bailey in the U.S. Bankruptcy Court for the District of Rhode Island in Providence late Monday approved the settlement agreement, which Gov. Lincoln Chafee called "an enormous milestone for the state."

Theodore Orson, the attorney representing Central Falls, said the case could serve as a national model. He cited Rhode Island's new law protecting public bondholders by requiring municipalities to guarantee lenders first rights to their property taxes and general revenue.

That law passed six weeks before state-appointed receiver Robert Flanders filed a bankruptcy petition on behalf of the city on Aug. 1.

"Chapter 9, I believe, can be used successfully if one of two things happens," Orson, a name partner in the Providence firm Orson and Brusini Ltd., said in an interview. "One, if other states pass similar laws similar to the municipal lien statute passed in Rhode Island, or two, if Congress amends Chapter 9 to provide municipalities to elect to give priority to general obligation bondholders."

Next, according to Orson, are discussions with two sets of school employee unions. Should an agreement be reached by mid-March, Orson envisions an exit from Chapter 9 by June or July. Lacking those agreements, he said, an exit could take several more months.

Central Falls, which has a population of 19,000, faced an \$80 million pension shortfall when it filed under Chapter 9. In December, Flanders and most retired police officers and firefighters reached the agreement, which calls for a 55% cut in pensions after five years.

Chafee will ask state lawmakers for a one-time \$2.6 million expense to fund transition payments over five years in order to allow retirees time to adjust to their reduced pension payments. Retirees would get combined pension and transition benefits, which will result in reductions of up to 25% of what they were receiving before the bankruptcy filing.

Should the General Assembly approve less than \$2 million for transition, participating retirees could opt out of the agreement, which 122 out of 133 signed.

Bill Brandt, the president and chief executive of consulting firm Development Specialists Inc. and chairman of the Illinois Finance Authority, said Flanders benefited from broad leeway.

"Chapter 9 is not the cutting edge for this matter," Brandt said. "Under Rhode Island law, the receiver has more power than the judges in bankruptcy court. My guess is that the judge used his good office much like a super mediator."

Bailey, assigned to the case from Boston, said the agreement will place Central falls on "substantially better footing," and called Flanders' accomplishments "rather remarkable."

Alan Gover, a partner at White & Case LLC in New York, said the parties negotiated more seriously, realizing there was bankruptcy court oversight. "In this case, we see Chapter 9 used as more of an environment for negotiation rather than litigation and hard decision-making. You may see more of a use of Chapter 9 for just that purpose," he said.

The agreement will be central to the city's five-year recovery plan as outlined by Flanders, a retired Supreme Court justice. The agreement, Chafee said, will mean a reduction of more than \$20 million in future pension payments due to the retirees.

The city stands to save more than \$1 million per year in annual payments to fund pensions, and reduce its current unfunded pension liability by 49%, to \$23.9 million from \$46.6 million.

"Bondholders are better off in an environment of compromise instead of one of fighting and impasse," Gover said.

Moody's Investors Service said last month that timely approval of the bankruptcy plan, improved funding for long-term liabilities, and a bankruptcy exit would help improve the city's rating, which it downgraded in June to Caa1 from B3, with a negative outlook. Orson said the pension agreement satisfies all three conditions.

Jonathan Henes, a restructuring lawyer at Kirkland & Ellis LLP, praised Flanders for achieving the compromise so quickly.

"This shows how a city can file Chapter 9, work out its issues and at the end of the day not have a negative impact on the bond markets. And when it does that successfully, a bond investor will want to invest in the city," Henes said. "I've never really believed that a Chapter 9 filing hurts the bond markets because the bond markets are pretty smart at realizing what cities are trying to do."

Chafee's administration also wants to move the locally administered pension plan into the state-run Municipal Employees Retirement System.

Flanders said in a court filing that the compromise was essential to protecting the city's access to the capital markets, as well as that of Rhode Island's other 38 municipalities and even the state's.

Rhode Island in November passed a law overhauling its state-run pension systems, and lawmakers are expected to consider legislation this year enabling cities and towns to do likewise.

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