

OPED: LESSONS FROM PUERTO RICO'S RESTRUCTURING

While the territory's Title III restructuring was unique, other municipalities can still gain important insights from the case.

BY DEAL CONTRIBUTORS

The following article was written by O'Melveny & Myers LLP's John J. Rapisardi and Peter Friedman.

It was a gratifying moment for us on Jan. 18 when U.S. District Court Judge Laura Taylor Swain approved the plan of adjustment for the Commonwealth of Puerto Rico's central government bonds and obligations. In doing so, she validated the work we have done over the past five years in representing Puerto Rico's elected government in a \$120 billion restructuring — the largest municipal bankruptcy in U.S. history.

Puerto Rico entered a bankruptcy-like proceeding in May 2017 with dangerously low liquidity, unsustainably high debt obligations, a stagnant economy and a pension system well past insolvency. The government has taken admirable steps to address these problems, and the plan of adjustment ensures extraordinary protections for the island's retirees while achieving significant debt relief for the government.

The five-year proceeding was unique — weathering hurricanes, earthquakes, political upheaval and a pandemic — but other municipalities can still gain important insights from the case.

As counsel to the government of Puerto Rico and three of its governors, our firm helped formulate the plan of adjustment, which aligns the commonwealth's interests with those of its creditors, retirees and counterparties. We faced an unusual challenge in working with the new Financial Oversight Board and Management Board for Puerto Rico (an entity Congress



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created, handing it financial functions that used to belong to Puerto Rico's elected government).

Ultimately, we gained the board's cooperation — along with bondholders' and monoline insurers' — to help our client achieve tremendous benefits. But none of these accomplishments would have been possible without Puerto Rico's government enacting legislation that brought its restructuring to a close. The government showed courageous leadership in making difficult decisions to protect its citizens.

In working through the issues, we learned some key lessons:

- Understand the rules of the game. Congress established the Oversight Board that dictated rules of

engagement for Puerto Rico, and bankrupt cities face similar control from state governments. It is critical that local governments contemplating bankruptcy understand how to operate in that context and also what it means to enter a court-supervised bankruptcy proceeding.

- Assert your rights. We won a landmark decision at the outset of the case, which gave the government a critical seat across from the Oversight Board in the courtroom and at the negotiating table. Securing such a seat will be vital for any town or city that finds itself at the restructuring table. Local governments cannot let a restructuring happen to them; they must ensure restructurings happen with them.

- Remember what you stand for. The government's goals were simple: Restructuring had to result in a workable debt-service plan without harming pensioners. Through the debt adjustment plan, the commonwealth went from \$35 billion of creditor claims to \$7.4 billion in new debt. But early versions of the plan proposed by the Oversight Board would have imposed an 8.5% cut on public pensioners receiving more than \$1,500 in monthly benefits. A pensioner should not have to suffer that. What's more, cutting retirees' pensions is counterproductive if those same retirees will then need public assistance.

- Be resilient, flexible, and listen. Resolving municipal bankruptcies requires input from all stakeholders. Do the work and be resilient. Fight when it serves the public interest, but be flexible if it helps attain your long-term goal. When the proposals were attractive enough, our client accepted them, making peace with parties it had battled for years. Bankruptcy is lengthy and expensive;

when the time comes to exit on good terms, seize it. In Puerto Rico's case, resolution was aided immeasurably by a team of federal judges who had been appointed to mediate an array of disputes. That team made sure that critical lines of communication remained open, even when the parties seemed far apart.

Of course, the work in Puerto Rico is not done. There are still issues to be addressed for Puerto Rico's utility company and certain municipal corporations. And Puerto Rico must build on government reforms to continue its return to the capital markets as a responsible borrower and regain the trust of its citizens. Ultimately, the citizens of Puerto Rico must be confident that their sacrifices will benefit their descendants.

Puerto Rico will still be hamstrung until Congress treats the commonwealth the way it treats each of the 50 states.

Many of its original financial problems stemmed from its colonial status: It must comply with federal standards without receiving parity in federal funding from Congress; Puerto Rico's people pay higher prices because of arcane laws; and its citizens are ineligible for many benefit programs including Supplemental Social Security Income. It was Puerto Rico's colonial status that permitted Congress to impose a federal oversight board on it — an indignity that could never be forced upon a state.

Our federal government must do its part to help Puerto Rico achieve equality and, in turn, its full potential.

We were privileged to assist Puerto Rico in its financial rehabilitation and restructuring. The lesson of Puerto Rico is that municipal restructurings are interactive, multi-faceted endeavors and that all efforts — political, transactional and legal — must be directed to serve the interests of the people first.