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Bankrupt San Bernardino to Impair Bondholders, not Calpers, in Exit Plan - City Attorney.

(Reuters) – Bankrupt San Bernardino will significantly impair its bondholder creditors while paying pension fund Calpers in full in a plan to be presented in May, City Attorney Gary Saenz said on Thursday.

San Bernardino has also not held any talks with its capital market creditors since September and has no immediate plans to do so before it presents its bankruptcy exit plan by a court-ordered date of May 30th, Saenz said.

Major creditors are viewed as less important creditors than Calpers, California's public pension fund, he said.

Capital market creditors in the San Bernardino bankruptcy include Luxembourg-based Europäische Pfandbrief-und Kommunalkreditbank AG (EEPK), holder of about $50 million in pension obligation bonds; Ambac Assurance Corp, which insures a portion of those bonds; and Wells Fargo Bank, the bond trustee and the flagship bank of Wells Fargo & Co.

Saenz said the city definitely intends to cut its debt to EEPK, Ambac and Wells Fargo under its bankruptcy plan, but in a way the judge will view as reasonable.

"Our bankruptcy plan will include an amount that is fair and reasonable to impair those creditors," Saenz said, referring to EEPK, Ambac and Wells Fargo. Until now, no representative has publicly said that the city intends to impair its bondholders.

San Bernardino, a city of 205,000, 65 miles east of Los Angeles, declared bankruptcy in July 2012 with a $45 million deficit. It is one of a handful of municipal bankruptcies that has been closely watched by the $3.6 trillion U.S. municipal bond market.

Bondholders and public employees want to understand how distressed cities handle their debts to Wall Street, compared with other creditors such as Calpers.

The future health of San Bernardino after it emerges from bankruptcy will depend on a workforce that has reliable pensions, Saenz told Reuters.

While impairing bondholders might impact the city's ability to borrow money at a later date, that is less of a concern to city officials than having a healthy pension plan, Saenz said.

San Bernardino struck a deal last year with the California Public Employees' Retirement System (Calpers), America's biggest public pension fund with assets of $300 billion, to pay it in full under any bankruptcy plan.

EEPK and Ambac sued San Bernardino this month, arguing that they should be treated as equal creditors to Calpers. Representatives were not immediately available for comment.

Saenz said the city will present its bankruptcy plan in May to give creditors a clear idea of how much the city can afford to pay them. The city was preparing for months of challenges and possible litigation from unhappy creditors after the plan is presented, he said.

"From their perspective, they see some impairment of Calpers as reasonable if they are going to receive a significant impairment," Saenz said, referring to EEPK, Ambac and Wells Fargo. "But we need to compare that argument to our ability to provide services for our city. And that needs a workforce. And you can't have a workforce without pensions."

Under the city's bankruptcy plan that is being drafted, cutting its debt to its pension obligation bondholders "will not have the same impact on the city post-banktruptcy if we impaired pensions," Saenz said.

Mediated talks between San Bernardino officials and its capital market creditors ended in September without agreement, Saenz, and a bondholder source familiar with discussions, told Reuters. Specific sums were discussed in mediation as to the extent to which the city wanted to cut that debt, but the parties ended the talks far from agreement, they said.

No conversations between the city and its capital market creditors have been held since and no further negotiations are scheduled, they said. The city has been ordered to produce a bankruptcy exit plan by May 30th.

Saenz said the city had been keeping a close eye on the bankruptcies of Detroit, Michigan, and Stockton, California. Both cities have had bankruptcy plans approved. In Stockton, Calpers was left untouched, and in Detroit pensioners emerged relatively unscathed, compared to Wall Street creditors.

BY TIM REID

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